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# COMMUNICATIONS ACT OF 1934

## Section 214

### Legislative Background

PREPARED FOR THE USE OF THE  
COMMITTEE ON INTERSTATE AND  
FOREIGN COMMERCE  
HOUSE OF REPRESENTATIVES  
AND ITS  
SUBCOMMITTEE ON COMMUNICATIONS  
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## LETTER OF TRANSMITTAL

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CONGRESS OF THE UNITED STATES,  
HOUSE OF REPRESENTATIVES,  
*Washington, D.C., April 30, 1979.*

HON. HARLEY O. STAGGERS,  
*Chairman, Committee on Interstate and Foreign Commerce, U.S.  
House of Representatives, Washington, D.C.*

DEAR MR. CHAIRMAN: Attached is a staff study on the legislative history of section 214 of the Communications Act of 1934. The study is the product of 9 months of extensive research and drafting by Kathleen Casey, minority staff assistant, under the supervision of Ronald D. Coleman, associate minority counsel. The study details the history of the development and application of the provisions of section 214, tracing its origin to railroad legislation.

It would be very useful to the members of the committee to publish this study as a committee print, especially since section 214 is a major element of current common carrier regulation that our subcommittee is reviewing during consideration of comprehensive communications legislation.

Sincerely,

LIONEL VAN DEERLIN,  
*Chairman,  
Subcommittee on Communications.*

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# COMMUNICATIONS ACT OF 1934

## SECTION 214

### LEGISLATIVE BACKGROUND

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#### I. INTRODUCTION

Section 214 of the Communications Act of 1934 establishes the regulatory charter over entry into common carrier communications, and subsequently, its industry structure. Section 214(a) states that no carrier shall construct, extend, or acquire a "line" unless it has first applied for and received an instrument of authorization from the Federal Communications Commission. The FCC's stated responsibility is to determine whether such entry would be in the public interest, convenience, and necessity. The Commission may issue notice of pending action on an application, commence a hearing procedure, and issue a formal ruling on the matter. The same requirement is applied before a carrier may discontinue, reduce, or impair service. Section 214(a) contains certain exemptions from the requirements of the section; that is, any terminal or branch line less than 10 miles in length, or any changes in plant, operation, or equipment that does not involve new construction and does not impair the adequacy of the service provided.

Section 214(b) establishes procedures for notice of pending action on applications; 214(c) permits the Commission to attach conditions on facilities authorizations (such as to limit the services which may be offered); 214(d) provides that the Commission may, after hearing, order a carrier to provide facilities, extend its lines, or to establish a public office.

Section 214 obligates the FCC to prevent the service supplier from unnecessarily extending, acquiring or abandoning lines. This scrutiny of corporate action is, in effect, a check on industry structure in the sense that it gives the Commission the discretion to regulate entry and effectively define the markets in which monopoly and competition may exist. It is also a major supplement to rate of return regulation in the form of a control on the addition of capital to the rate base. This precludes rate base inflation, that is, excessive or unwise investments which the rate of return ceiling does nothing to prevent.

This authority was meant to avoid economic waste and insure over-all service continuity through several underlying schemes: It was to protect the subject carrier and other carriers already occupying the field from revenue diversion and instability. Second, it was to protect the public obligation to guarantee a profit to the telephone or telegraph utility. It was also to reinforce the status of common carrier with the guaranty of local service continuity once the requisite lines and equipment have been put into place. This report constructs the circumstances

that required this statutory imposition, and its history of interpretation and treatment.

The Section 214-type "solution" was no novelty in 1934; it derived from the Transportation Act of 1920. Therefore, this report traces the evolution of corporate practice and regulatory policy in the railroad industry to document the existence of problems in industry structure that that act was intended to resolve. This is followed by excerpts from the official documentation of the enacting legislature's purpose.

These sources indicate the extent of public awareness of problems and the example and experience of action taken elsewhere, i.e., the courts and State legislatures. Hearing and debate records provide evidence from several viewpoints of the scope of public consensus with the authorizing Congress. Opinion may vary as to the existence of a problem, and hence of the need for policy, or as to interpretation and appropriate legislative solution.

Because it was obviously transplanted from railroad law, the legislative purpose of section 214 was somewhat less integrated than its predecessor with the perspective of existing facilities, services, and industry structure. Substantial background is discussed on the state-of-the-art of telephone service delivery and of existing communications utility law both at the Federal level for service to overseas points and in the States. It is apparent, for instance, that domestic service was based on a relatively uncomplicated network of "lines." Sophisticated techniques of delivering new capacity were in the experimental stage or were yet to come; and since regulation traditionally tends to lag after the pace of technological advance, the law reflected this status quo. Furthermore, section 214 was preceded by similar language in State utility law, as a method of limiting duplication of telephone exchanges and intercity lines. In contrast, the international services had been integrated with the opportunities of high-frequency radio under a rather liberal scheme of law that was reenacted into title III of the Communications Act.

International communications had been performed for several decades by record carriers competing in the use of submarine cables. Point-to-point radio technology was developed at first for ship-to-shore service; and its long-distance capacity was refined during World War I. The introduction of service was motivated both by the cost efficiency of the radio mode and a policy directive in the Radio Act of 1927 that radiotelegraph carriers be allowed to freely compete with the established cable industry. A thorough legislative history of the Radio Act and its transposition into the Communications Act is not within the scope of this report. This early history is provided, however, in order to add perspective to the FCC's handling of service authorizations for the international sector.

When enacted in 1920, the legislative accountability of the railroads for market entry and major capital outlays was relatively unprecedented; and by 1934 there were several instances of court definition of the purpose and meaning of the words in the statute. In the absence of similar treatment of section 214, the FCC tended to refer to these cases for administrative guidance.

The FCC's initial authorization proceedings are given extensive treatment in casebook fashion. This explains the rationale by which it asserted jurisdiction over capital acquisition in the domestic sector,



and over both domestic and international market entry. The standard of investment control for rate base purposes was not devised for international service authorization until transatlantic submarine cables came into use much later, during the 1960's.

These early rulings, tested both in the courts and in subsequent administrative practice, have formed the basis for present-day regulation of competition and capital investments in both sectors. This report concludes with an explanation of pivotal, recently settled rulings in order to demonstrate this theme.

## II. "SECTION 214" OF THE TRANSPORTATION ACT OF 1920

### A. *Early railroad law*

The first form of systematic railroad regulation was the enactment of general incorporation laws and the creation of railroad regulatory commissions in some New England States during the 1830's and 1840's, the initial years of railroad building. All of the early railway companies had received individual charters from the States by special legislative enactment.<sup>1</sup> The power granted to the commissions was usually supplementary to the issuance of State charters, and served to overcome the futility and confusion of contradictory charter regulation. These "free railway laws" actually exerted very little control. They concerned themselves mostly with matters of safety, taxation, and the gathering of accounting and statistical data; and in but few cases were there attempts at ratemaking.

A great disadvantage of these pre-Civil War statutes was that projects could be undertaken without their effect on other lines, thus increasing the risks and speculation inherent in the trade. Before the adoption of the railway laws, this danger had been an important consideration in the assignment of charters. The corporation had been obliged to insure that the project at issue was in the interest of the State as a whole and that it would not injure other railroads. In some jurisdictions an attempt was made to remedy this situation by requiring a certificate of public convenience and necessity from a court or commission before a new railroad could be constructed.<sup>2</sup> The neglect on the part of the framers of most State laws to include this type of provision was one factor which contributed to the great deal of overinvestment during the railroad building period in the United States.

One other noteworthy cause for this extravagance was the incidence of substantial subsidy of construction. Beginning in 1850, land grants were the most important form of Federal aid, contributing to the finish, in 1869, of the first transcontinental railroad. A common form of local financial aid was subscription to railroad stock. Many private citizens went so far as to mortgage their farms and homes for railroad investment. Railroad corporations were also granted outright donations in the form of cash, securities, rights-of-way, material, equipment, and labor. Furthermore, county and municipal governments offered loans and the guaranty of bonds, which were usually financed by public debt.<sup>3</sup>

<sup>1</sup> D. Philip Locklin, *The Economics of Transportation*, 6th ed. (Homewood, Ill.: Richard D. Irwin, Inc., 1966), p. 100.

<sup>2</sup> *Id.*, p. 101. See, e.g., *People of the State of New York ex rel. New York Central and Hudson River Railroad et al. v. Public Service Commission of the State of New York*, 227 N.Y. 248 (1895): "The provision added to the Railroad Law in 1892, requires a railroad corporation to secure from the railroad commissioner a certificate \* \* \* before construction \* \* \* The object was to permit the railroad commissioners to prevent wasteful competition and public disaster by the construction of public roads through localities which already were adequately served \* \* \*". (Reference omitted.)

<sup>3</sup> A not uncommon circumstance was that of Watertown, Wis. With a population of 7,553, the township incurred a railroad debt of \$750,000, nearly \$100 per capita. Stuart Daggett, *Principles of Inland Transportation*, revised ed. (New York: Harper & Brothers, 1934), p. 102.



For the purpose of these endeavors, the interests of the public and the corporations were considered to be the same. The public wanted railroads, and the firms wanted to build them. Railroads were becoming a vital part of the infrastructure of the national economy, and of the economic future of communities of every size. Consequently, people were willing to pay almost any price for them.

Following closely on their completion, however, the private corporations evidently began to demonstrate ruthless procurement instincts. The public, of course, expected the lowest possible rates from these enterprises whom it had so generously aided; and its benevolence soon shattered. Public outcry followed on such methods as inflated rates, preference to favored dealers, and regional discrimination, especially against noncompeting points. "Absentee ownership" by eastern capitalists aggravated the situation, as did the conduct of unscrupulous promoters as stock values declined to as low as worthless.

Part of this strong anti-railroad feeling manifested the "agrarian" ideology of the Granger movement. While corporate prejudice had existed in parts of the country as early as 1850, it was the Granger movement that resulted in the first positive legal control over the railroad industry, particularly in Illinois, Iowa, Wisconsin, and Minnesota.<sup>4</sup> The experience of the Granger States and of those that passed laws in imitation of them became a fund of knowledge to the Congress that drafted and passed the original Interstate Commerce Act (ICA).<sup>5</sup>

The act of 1887 was significant as an assertion by the Federal legislature of the legitimacy of the doctrine that the railroads were subject to public control. The notion that private business was to submit to external authority was still fairly "radical" during this period; but its constitutionality had been repeatedly upheld by the Federal courts.<sup>6</sup>

The 49th Congress was motivated by factors additional to court pronouncement and the precedent of State initiative. The immediate reason was evidence that, in the absence of Federal law, State-by-State regulation would allow a great deal of traffic to escape legislative control.<sup>7</sup> Another source of instruction lay in England, where a respectable body of statutory law existed.<sup>8</sup> Finally, the Congress was pushed forward by an aroused public opinion offended by monopolistic railroad practices. Resolutions calling for study of the idea of interstate regulation were presented to Congress throughout the 1870's and 1880's, the time that the State laws were being debated and passed. Proposals for legislation appeared in every session since as early as 1868, although none were acted on for years.

<sup>4</sup> Locklin, *op. cit.*, n. 1, p. 198.

<sup>5</sup> Act of Feb. 4, 1887, ch. 104, 24 Stat. 379.

<sup>6</sup> See *Munn v. Illinois*, 94 U.S. 113 (1876); *Chicago, Burlington and Quincy Railroad v. Iowa*, 94 U.S. 155 (1876); *Piek v. Chicago and Northwestern Railroad Co.*, 94 U.S. 164 (1876); *Winona and St. Peter Railroad Co. v. Blake*, 94 U.S. 180 (1876).

<sup>7</sup> See *Wabash, St. Louis and Pacific v. Illinois*, 118 U.S. 557 (1886). While the Court did not deny its previous rulings that there were instances in which State rules might be applied to freight crossing its boundaries, it decided here that regulation of rates on interstate carriage must be regarded as exclusively within the field of Federal authority, and could not safely be remitted to local action.

<sup>8</sup> Long before Federal legislation was even thought about in the United States, the Railway and Canal Traffic Act of 1854 was enacted with much the same type of provisions as the ICA was to contain.

Beside endowing discretionary, although limited, administrative authority to the new Interstate Commerce Commission (ICC), the act prohibited pooling arrangements in reflection of the popular view that enforced competition was the best protection against unreasonable rates.<sup>9</sup> There was considerable opposition to this provision from those who saw that pooling was necessary to prevent destructive competition. The legislature, however, fearing railroad monopoly, was unwilling to permit it.<sup>10</sup> It was to this enactment that additional provisions were attached by the predecessor language of the Communications Act of 1934, and, of particular interest, of section 214 of that statute. What follows is a presentation of evidence demonstrating the intent of the 1920 amendments to the Interstate Commerce Act, and tracing the conversion of section I(18)-(22) to section 214. Included is a brief discussion of the history and purpose of the attending legislation, with an emphasis on that related to communications.

#### *B. Section I(18)-(22)*

The passage of the new railroad legislation was a response to the reasoning, slowly evolved after 1887, that competition might be extravagant and wasteful, and that it could result in unnecessary duplication of railway facilities and the impairment of the revenues of needed lines. The occasion for its enactment was the transition of railroad ownership from wartime operation by the Federal Government back to the private sector. The English used the same opportunity to nationalize their entire inland transport system. Likewise, the U.S. Congress at this time reviewed its entire policy of rail regulation.

The total scheme of the act was designed to answer complaints that the regulatory system was restrictive, did not do justice to conditions of rising costs, and encouraged destructive competition among the railroads. The main intent of the act was to improve the financial position of the railroads as a group, while avoiding conferring unnecessarily high returns on the strong companies. The primary method was a directive to the ICC from Congress that a plan be drafted for the consolidation of the Nation's railroads into a limited number of systems of comparable efficiency, profitability, and financial strength.<sup>11</sup> It was not true, however, that a complete reversal of policy occurred. The Commission was to allow pooling arrangements when they did not "unduly restrain competition."<sup>12</sup> Consolidation was to take place in accordance with the plan, during the preparation of which Congress specifically required that "competition shall be preserved as fully as possible."<sup>13</sup>

As mentioned, pooling had previously been forbidden for fear of allowing groups of firms to attain an unseemly amount of market power; similarly, mergers had been attacked under antitrust laws. The changes initiated by the Transportation Act do indicate, despite their qualifications, a significant reversal of the prior faith in the market-

<sup>9</sup> Locklin, *op. cit.*, n. 1, p. 212.

<sup>10</sup> *Loc. cit.*

<sup>11</sup> Alfred E. Kahn, "The Economics of Regulation: Principles and Institutions" (New York: John Wiley & Sons, Inc., 1971), II, 79.

<sup>12</sup> *Loc. cit.* See act of Feb. 28, 1920, ch. 91, 41 stat. 481.

<sup>13</sup> *Id.*



place to induce fair practices and earnings sufficient to attract investment. The act directed the Commission to take a more active role in directing both the industry's structure and its performance. The inclusion of a provision giving control to the ICC over extensions and abandonments of lines was consistent with this design.

The report of the Interstate Commerce Commission to the Congress, submitted in 1918, recognized a need for a new railroad competition policy. One of its four recommendations was "the limitation of railway construction to the necessities and convenience of the government and of the public and assuring the construction to the point of these limitations."<sup>14</sup> This option was provided for in "a new provision which prohibits the construction or abandonment of lines of railway except upon the authority of the regulating tribunal."<sup>15</sup> The amendment of Section I of the Interstate Commerce Act by Section 402(18)-(22) of the Transportation Act invested control to the Commission over the construction and abandonment of railway property. It was patterned after such certification requirements as existed in state law. The scope of the Commission's authority was the issuance of certificates of public convenience and necessity after application, hearing, and notice to the appropriate State authority. Its proceedings were to relate to the construction of new lines, to the acquisition or operation of any line of railroad or its extension, and to the abandonment of all or any portion of a line of railroad or its extension. This include those lines which, although lying wholly within one State, still affected interstate commerce, even though built by corporations not previously subject to the ICA.<sup>16</sup> These provisions applied only to railroads even though section 400(3) of the same amending act specifically defined common carriers to include, *inter alia*, telegraph, telephone, and cable companies operating by wire or wireless.<sup>17</sup>

The purpose of the certification requirement was to prevent the needless duplication of existing routes and the construction of unprofitable lines. Senator Cummins, chairman of the Interstate Commerce Committee and sponsor of the Senate's version of the bill, defended the language of the provision in the following manner:

I do not remember how many States have legislation of this character, but there is a very considerable number of States which for the protection of their people and the better regulation of their commerce have adopted provisions substantially like the one now sought to be eliminated from the bill.

It presents to the country a question which ought to be considered and ought to be decided without passion or prejudice, and ought to be decided without respect to the effect which it is supposed it would have upon any particular part of the United States. If there is any one thing which the transportation system of the country taken as a whole, is now

<sup>14</sup> Testimony of Edgar Clark, Commissioner, Interstate Commerce Commission, U.S. House of Representatives, Committee on Interstate and Foreign Commerce, *Hearings on H.R. 4378, Return of the Railroads to Private Ownership*, 66th Cong., 1st Sess., I, 53 (1919) citing <sup>15</sup> *Id.*, p. 54; see Act of Feb. 28, 1920, ch. 91, 41 Stat. 477-78; 49 U.S.C. I 18(a)-(e), Ia (1)-(11).

<sup>16</sup> See *Texas & New Orleans Railroad Co. v. Northside Belt Railway Co.*, 276 U.S. 475, 479 (1928). The court felt that as long as the railroad confined its operations to intrastate commerce, construction without a certificate would not violate federal law.

<sup>17</sup> Act of Feb. 28, 1920, *op. cit.*, n. 12, at 474.

suffering, it is from the unguided, uncontrolled right of owners to build railroads wherever they may see fit to build them and wherever they can avail themselves of an opportunity to sell at a profit the securities based upon the supposed construction.

The railways of the United States are not built where they should be built. Everybody understands that. A great many have been built that never should have been constructed. We are now under the disadvantage of having developed a system which must be maintained because communities have been built up along railways, and their interests cannot be disregarded in the regulations which we shall adopt. [This] has arisen because of the building of railways simply to make money out of their construction and without regard to the possible profit of their operation.<sup>18</sup>

John J. Esch, the chairman of the House of Representatives' Interstate and Foreign Commerce Committee, also articulated the purpose of Federal review of railroad construction:

[O]ne cause of the so-called "weak sister" has been the unrestricted right of railroads to be built wherever their proprietors thought fit. As a result of this unrestricted right we find in all States of the Union cases where, after a road has been built and well maintained and has gotten its traffic well established, another road puts in a parallel line with a result that instead of one strong road doing the traffic we have two weak roads, so they have to charge the same rate between competitive points and we burden the public by compelling it to sustain two weak roads when one strong road would have been sufficient.

How does the bill stop that? In this way: Before a road or an extension thereof can be built it must get what is called in this bill a certificate of convenience and necessity from the Commission as a condition precedent to the building of a single rod [sic] or the extension of a new line \* \* \*.

This is not a new law. Several of the States have this kind of law now, notably the State of New York and the State of Wisconsin, and in other States the law has worked successfully. It has prevented the construction of new lines that could not by any possibility have any hope of meeting operating expenses, not to say anything about profits. It would prevent the construction of some of these short lines which may have no hope of ultimate financial success. In every way we have felt that this provision would lessen the number of "weak sisters," would prevent the creation of any new ones, and would strengthen the existing lines. We can get better service by strengthening the existing lines than by creating a rival or parallel line which would diminish the ability of the first line to make further improvements or betterments.<sup>19</sup>

<sup>18</sup> 59 Cong. Rec. 748 (1919); see also Rogers MacVeagh, "The Transportation Act of 1920, Its Sources, History, and Text" (New York: Henry Holt & Co., 1923), p. 221.

<sup>19</sup> 58 Cong. Rec. 8316 (1919); MacVeagh, *id.*, p. 220.

Section I (18)-(22) was therefore intended to protect existing lines from competition to some extent. The causes and deleterious effects of uncontrolled duplication were illustrated during a hearing exchange with a commissioner of the ICC:

The CHAIRMAN. Would the exercise of this power on the part of the Federal Commission in any way tend to stabilize the securities of the company that had been given a certificate?

Mr. CLARK. It seems to me inevitable that it would have that tendency and that effect. The principle underlying this is that a carrier, having been given a franchise to enter a field, ought to be protected against unnecessary and wasteful competition of the rival carriers.

You will remember a few years ago as an instance of this, there was the keenest kind of rivalry between the roads that were commonly known as the Harriman interests and the Hill interests in the Northwest. The Harriman lines scouted the idea of building a line \* \* \* which they said was not worth building into; but then Hill had a different idea after a few years, and he started to build in there, and immediately the Harriman lines, with the most feverish haste and lavish expenditure, started and constructed a parallel line, so that that territory which was thought not worth serving with one railroad was served with two expensively built railroads under rival conditions so that cost was largely disregarded, and now the territory and the public have two roads to support.<sup>20</sup>

The capitalization problems that the provision was to help correct had grown from speculation and poor management as well as destructive competition among carriers. Administrative review prior to construction would, it was felt, encourage investment in railroad facilities to aid in stabilizing the failing credit worthiness of the system:

It will aid very materially in securing the funds necessary for construction, and it is not likely that the old system of construction will be resorted to in the future. The people are not willing, and they will never be willing, in my opinion, to make large grants of public lands, to give enormous donations, to secure the construction of railroads; and if this conclusion be correct, then the provision \* \* \* ought to stay in the bill because it recognizes the power of the Federal Government to pass upon the question.<sup>21</sup>

The certification feature was regarded as a compliment of the planning and consolidation elements of the bill. It was felt that if the Federal Government were to direct the reorganization of industry structure, it should also have a controlling interest in the issuance of certificates to parties which carried business destined for interstate traffic. This logic was expressed during Senate floor debate:

It is in harmony with some of the general and important features of the bill, particularly those relating to the consoli-

<sup>20</sup> U.S. House, op. cit., n. 15, I, 62.

<sup>21</sup> Remarks of Senator Robinson, Member, Committee on Interstate Commerce, 59 Cong. Rec. 863 (1919).



dation of railway lines and systems. If you strike out this provision you weaken the consolidation features of this bill \* \* \* if we are to reorganize the railroads and put them on a sound financial basis, we ought not to leave it in the power of anyone in any locality to undo the very thing we are trying to do \* \* \*.<sup>22</sup>

The chairman of the House committee explained the purpose of the requirement of ICC approval prior to the abandonment of lines:

Railroads sometimes surrender the rights granted by their charter. The traffic is not what they expected, business conditions change, the natural resources which they thought first to get out to the open market become exhausted. There is no power now to restrain abandonment under Federal law. Railroads in many States can do as they will. We provide some control over the matter of abandonment so that cities and villages that have been built up on these lines can be given due consideration by the regulatory body before the order for abandonment is issued. Or given such control to the Commission to investigate the situation and determine the facts.<sup>23</sup>

The abandonment question was elaborated on by the National Association of Railroad and Utilities Commissioners:

The law dealing with the power of the railroads to abandon service or track is quite debatable. Some courts have held that where a common carrier has taken out a charter to do business between two terminals that it shall not abandon its track. Other courts have held that where the company cannot profitably be employed the court may permit abandonment of that track \* \* \*.

In my own experience as a commissioner I have passed upon a number of these abandonment cases. In some of those cases we permitted the abandonment to take effect at some future period which would make those who have farm produce and timber ready to haul out during that season and had to get it out before the road was taken away. In others, the evidence showed clearly that the company was not operating at a loss and that they had a public service to perform.<sup>24</sup>

These remarks are evidence of the point of view that a carrier creates for itself the common carrier obligation of service to a locale that has become dependent on railroad transportation. This onus was also tantamount to the power gained by the Commission to compel new construction. Besides the certification requirement in paragraph 18, section I provided through paragraph 21 that the ICC may, after a hearing, "authorize or require by order a carrier by railroad subject to this act \* \* \* to provide itself with safe and adequate facilities for performing as a common carrier its car service as that term is used in this act, and to *extend its line or lines*." (Emphasis supplied.) The required extension is conditioned to be reasonably required in the interest of "public convenience and necessity" and the expense in-

<sup>22</sup> Remarks of Senator Robinson, 59 Cong. Rec. 862, 863 (1919); quoted in part in MacVeagh, op. cit., n. 18, p. 223.

<sup>23</sup> 58 Cong. Rec. 8318 (1919); MacVeagh, op. cit., n. 18, pp. 220-21.

<sup>24</sup> Testimony of Charles E. Elmquist, president, NARUC, U.S. House, op. cit., n. 15, II, 1607.



volved must not "impair the ability of the carrier to perform its duty to the public." The purpose for this power of compulsion was given some treatment in the ICC's report to Congress:

The thought underlying \* \* \* this suggestion is that a railroad having been permitted, by public franchise and the powers that go with it, to build into a given territory, it should be required to properly serve and develop that territory. And in developed territory it is important to provide for the extension of short branch or spur lines or spur tracks to communities and industries that should be served and that can furnish sufficient traffic to justify such extension.<sup>25</sup>

Finally, the efficiency of railroad construction was linked directly to section 15(2) of the bill. It was here that the "rule of ratemaking," since refined and known as rate-of-return regulation, was first legislatively enacted to control return levels, based on the aggregate value of railway property. If the public was to commit itself to a policy of paying rates which would yield to the carriers an adequate return, it seemed obviously desirable to prevent the construction of unnecessary lines.<sup>26</sup> All the foregoing effort—the attempt to prevent duplication and destructive competition, and to integrate the certification intent with the law's design for coherent management—was given urgency by the prospect that a serious and systematic ratemaking proposal was to be part of that same scheme.

As the field of regulatory economics developed, the Averch-Johnson effect was devised as a model to explain a principal negative incentive that rate-of-return regulation creates for the utility. Regulation since the early part of the century has typically concentrated only on a specified average return on capital investment. Without supplemental oversight, the regulated company may invest excessively in capital facilities (whether less efficient than labor and hence more expensive), rather than reduce costs, because it can expect to earn more profit from its total operations, provided it does not exhaust the total market for its services. Hence, the rate of return is adjusted to the appropriate percentage of the aggregate rate base, and the cost of unneeded investment is passed on to ratepayers (this may influence the company in the direction of service quality improvements rather than actual negligence).<sup>27</sup> This concept has major implications for any regulatory program such as (18)–(22) or section 214. There was obviously some understanding of this in 1920, as the linkage of section I(18)–(22) with section 15(2) effectively gave the ICC the authority to control additions to the rate base. This pertains also to the FCC's administration of section 214.<sup>28</sup>

\* \* \* \* \*

By no means was there complete agreement on the merits of the power of compulsion or the mandatory certification requirement itself.

<sup>25</sup> *ICC v. Oregon-Washington R. Co.* 288 U.S. 14, 36, footnote (1932), citing *Report of the Interstate Commerce Commission to the Congress*, 1918, p. 2.

<sup>26</sup> Locklin, *op. cit.*, n. 1, p. 233.

<sup>27</sup> Kahn, *op. cit.*, n. 11, I, 24–25.

<sup>28</sup> Although there is no word in the Communications Act of rate of return regulation. The Commission relies primarily on sections 201(h) and 202(a) in determining lawfulness of charges; the rate of return method is an inherited administrative one for insuring that the aggregate of all receipts acquired for services provided return a profit to the utility's owners.

Much doubt was expressed in legal circles as to the constitutionality of the power given to the commission in paragraph 21. It was felt that unless such an action was accompanied by an absolute guaranty of earnings, it would amount to the taking of property for public use without just compensation. Only once has the ICC issued an order requiring a carrier to extend its lines, although a number of similar cases had been before it which had been refused. In 1929, it directed a subsidiary of the Union-Pacific Railroad Co. to construct a cross-State line about 187 miles long, at an estimated cost of \$9 million. This order was subsequently set aside by the Supreme Court in *Interstate Commerce Comm. v. Oregon-Washington Railroad & Navigation Co.*<sup>29</sup> The express purpose of the requested extension was to provide facilities for expeditious shipment of commodities, and to develop and enhance the area's natural resources. The Court observed:

The phrase "and to extend its line or lines" is part of a single sentence committing to the Commission the power to require carriers to provide safe and adequate facilities for car service as defined in the act. The reasonable conclusion is, therefore, that the extensions mentioned have to do with car service, and are not intended to create a wholly independent area of jurisdiction. In the proviso the furnishing of facilities and extension of lines are blended as belonging to a single class. We should expect, if the Congress were intending to grant to the Commission a new and drastic power to compel the investment of enormous sums for the development of service of a region which a carrier had never theretofore entered or intended to serve, the intention would be expressed in more than a clause in a sentence dealing with car service.<sup>30</sup>

The Court discerned "[n]o intimation [in the legislative history of the Transportation Act] \* \* \* that carriers should be required to build into territory they had not undertaken to serve" by license or franchise.<sup>31</sup> This construction was supported by a brief analysis of the relevant constitutional issues:

The railroads, although dedicated to a public use, remain the private property of their owners, and their assets may not be taken without just compensation. The Transportation Act has not abolished this proprietorship. State courts have uniformly held that to require extension of existing lines beyond the scope of the carrier's commitment to the public service is a taking of property in violation of the Federal constitution. Decisions of this Court will be searched in vain for the announcement of any principle of constitutional interpretation which would support the order of the Commission.<sup>32</sup>

As to the viability of the certification requirement itself, one Member of Congress argued wholly against paragraphs (18)–(22), saying that a locale desiring a railroad facility is best qualified to determine its own needs. The argument disassociated the present from the experience of the past by stating that the local populace would not likely

<sup>29</sup> Op. cit., n. 25.

<sup>30</sup> Id., at 35.

<sup>31</sup> Id., at 36.

<sup>32</sup> Id., at 40–41.

overinvest or be exploited by speculation, since it was provided in the bill that the issuance of securities was to be authorized and guaranteed by the Federal Government. Furthermore, it was pointed out, although most of the northeast and east had since become standardized and developed, the rest of the country was distinguished by vast, underutilized territory. This argued for responsible community initiative, rather than what was regarded as an indiscriminate and inhibiting certification requirement. In the Member's opinion, there existed more trouble from an inadequacy of rail facilities than from any other cause, and the provision would "grind railroad construction to a halt."<sup>33</sup> This same concern had been expressed before the House committee drafting the bill:

[W]ith respect to the extension of railroads or the building of railroads \* \* \* I know of no problem which requires correction by this enactment \* \* \* I doubt if there are enough lines of railroad now, if our country continues to grow \* \* \*. For example, on the Northwestern line to \* \* \* Wyoming, and on some the lines in South Dakota the service was extremely bad, so bad that it was difficult to handle livestock safely over those lines at all \* \* \*. The central-western country is served almost altogether by the transcontinental lines, and unless there is some provision made for building railroads into that country it will remain unpopulated and unproductive \* \* \*.<sup>34</sup>

Finally, many parties regarded paragraphs (18)–(22) as a fundamental part of a bill that was intrusive and unacceptable in any respect. A fairly typical comment was the following:

The Commission has only negative and restrictive power, and we think that when these extensions of administrative power are conferred upon any tribunal, it is only just to the subject of that regulation that some limit upon the exercise of that power would be laid down by Congress. \* \* \* You propose not only to regulate the issue of railroad securities \* \* \* [you] require extensions of their trunkline railway systems \* \* \*. This reaches the limit of constitutional authority \* \* \*.

The point I make immediately is \* \* \* to call to the attention of the committee that when you are giving to the Commission not only the power of life and death through the stoppage of rates and the control of rates, but propose to displace the corporate management in broad fields within which it has formerly exercised its discretion, and will thus change the original undertaking assessed by the stockholders in entering into that enterprise, you are giving such sweeping, drastic, and unlimited powers to the Interstate Commerce Commission as to make it necessary for you in some way to provide by a definition of policy which will retain that such wide power shall be exercised only under conditions that will result

<sup>33</sup> Remarks of Representative Smith, 59 Cong., Rec. 746–47 (1919).

<sup>34</sup> Testimony of S. H. Cowan, attorney, American Livestock Association, U.S. House, op. cit., n. 14, I, 855.



in a reasonable return, and not in a lawsuit for a return one point more than confiscation.

To say that a carrier shall be required to expend \$50 million or \$100 million and then remain in the bread line before the Interstate Commerce Commission in order to receive a reasonable return upon the investment it has made, Mr. Chairman, is going too far in the process of regulation.<sup>35</sup>

\* \* \* \* \*

The goals that the Congress sought were not plainly expressed by the words used in the language, requiring subsequent explanation by courts. This repeated statutory construction brought about an extensive case history of the legislative intent in Section I (18)–(22). Most plaintiffs requested that an injunction be applied against the action of construction until a certificate was obtained from the Commission, and in at least one case,<sup>36</sup> the legality of the Commission's authority was the focus of contention. It was invariably held that Congress had invested the Commission with the power to determine the facts of each instance, and to exercise its judgement as to whether a certificate was required.

By the early 1930's, the statutory purpose of section 1(18) had received generally two court interpretations. The certification requirement was most often distinguished as the regulation of competition so as to insure a viable service:

“[E]xtension” and “industrial track,” as used in paragraphs 18 to 22, is furnished by the context and by the relation of the specific provisions here in question to the railroad policy introduced by the Transportation Act of 1920. By that measure, Congress undertook to develop and maintain, for the people of the United States, an adequate railway system. It recognized that preservation of the financial resources of individual carriers, is a matter of national concern; that the property employed must be permitted to earn a reasonable return; that the building of unnecessary lines involves a waste of resources and that the burden of this competition between carriers may result in harm to the public, as well as in benefit; and that, when a railroad inflicts injury upon its rival, it may be the public which ultimately bears the loss.<sup>37</sup>

\* \* \* \* \*

New construction by an existing carrier might periodically affect the public by financially hampering its function in furnishing an adequate interstate service to the public; by invading the territory already adequately served by another carrier and thus injuring one or both of these by causing an increase in group rates or by other ways.<sup>38</sup>

The Supreme Court was in one instance obliged to determine whether the Commission was acting lawfully when it authorized con-

<sup>35</sup> Testimony of Alba B. Johnson, president, Railway Business Association, U.S. House, id., I, 1037, 1039.

<sup>36</sup> See, e.g., *Colorado v. U.S.*, 271 U.S. 153 (1926).

<sup>37</sup> *Texas & Pacific Ry. v. Gulf, Colorado & Santa Fe Ry.*, 270 U.S. 266, 277–78 (1926) (references omitted).

<sup>38</sup> *Missouri-Kansas-Texas R. Co. v. Northern Oklahoma Rys.*, 25 F. 2d, 689, 691 (1928) (cert. denied, 278 U.S. 610).

struction so as to provide to a coalmining region a choice among carriers for shipment of the product. The Court recognized, citing previous ICC findings, that the Congress of 1920 wished to balance its concern about duplication with a recognition that competition was not in all cases harmful. In so doing the Court implied the second interpretation of section 1(18), that is, rate base regulation. It was necessary to preclude excessive investment in the construction and operation of facilities which were not needed to insure adequate service, and for which a Commission-administered reimbursement (plus a "reasonable" profit) was to be expected from its revenues:

Undoubtedly the purpose of these provisions is to enable the Commission, in the interest of the public, to prevent improvident and unnecessary expenditures for the construction and operation of lines not needed to insure adequate service. In the absence of a plain declaration to that effect, it would be unreasonable to hold that the Congress did not intend to empower the Commission to authorize construction to new lines to provide for shippers such competing service as it should find to be convenient or necessary in the public interest. Indeed, section 6(4) of the act, which authorizes the Commission to prepare a plan for the consolidation of railway properties into a limited number of systems, clearly discloses a policy on the part of Congress to preserve competition among carriers. \* \* \* And the Commission has recognized the advantages of competitive service to shippers especially in respect of a diversified car supply for the shipment of coal and lumber; it suggests the possibility of failure of operation from various causes, that under some circumstances competition operates to stimulate better service and that reasonable competition may be in the public interest.<sup>39</sup>

The court reasoned that the imperative of cost-cutting would occur under the liability of market alternatives rather than under an accounting to an administrative presence. Competition would offset to some extent the rate of return rights of private investments dedicated to public utility resources. This is an interesting twist to the originally intended relation of 1(18)-(22) to the rate of return function, that is, a virtually absolute prior governmental veto of management investment decisions as a check on the public obligation to a carrier's return.

These cases and others like them enabled the lower Federal courts to rely on a great deal of antecedent in reviewing the fundamental purpose of 1(18):

The underlying purpose of the provision contained in paragraph (18) of the act forbidding the construction without first obtaining a certificate of convenience and necessity was to prevent improvident and unnecessary expenditures for the construction and operation of lines not needed to insure adequate service; to protect interstate carriers from weakening themselves by constructing and operating superfluous lines,

<sup>39</sup> *Chesapeake & O. Ry. v. U.S.*, 283 U.S. 35, 37-8 (1931). (References omitted.) See also *Transit Commission v. U.S.*, 289 U.S. 121 (1933).

and to protect them from being weakened by another carrier operating in interstate commerce a competing line not required in the public interest; and to preserve well balanced competition among competing carriers, that being deemed in the public interest.<sup>40</sup>

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<sup>40</sup> *Union Pacific R. Co. v. Denver & Rio Grande Western R. Co.*, 198 F. 2d, 854, 859 (Ninth Circuit, 1952).



### III. THE COMMUNICATIONS VERSION OF I(18)-(22)

#### *A. Industry structure and regulation prior to 1934*

##### *1. Domestic common carrier*

The first Federal entry into the regulation of the domestic industry was the enactment in 1866 of the Post Roads Act. This statute allowed for the grant of franchised rights-of-way for the construction of telegraph poles and lines, primarily in association with railroad tracks and public thoroughfares. Much like that of the railroads, this subsidy represented a policy of stimulating the growth of communications facilities. However, never in the history of common carrier communications did there evolve the degree of investment and wholesale risk on the part of the various levels of government as occurred during the growth of railroad service.

What little State public utility law existed into the early twentieth century was handled mostly by franchise, with stipulations regarding maximum rates and certain aspects of service. As the domestic industry grew, Western Union achieved dominance in telegraph during the 1870's through mergers with its competitors. It remains the main source of telegraphy to the present day, with the American Telephone & Telegraph Company, Inc., becoming its counterpart for voice telephone service.

A.T. & T. was organized in 1885 as the central and controlling company of the Bell System, several years after the invention of the telephone and the incorporation of the American Bell Telephone Co. It has since grown into a role as the major planning authority and manufacturing source for the development of a nationally coordinated telephone system. It provides local exchange service in concert with several hundred independent local companies; and Bell Long Lines manages the long-distance intercity network. This service is a complete contrast to the fragmented development of the railroad system, in which each regional and local corporation provided a fraction of the total service of moving people and freight nationwide. Never did the requisities for rational, end-to-end planning of railroad performance develop, either before or after the passage of the 1920 act.

(a) *The network.*—The construction of manual switchboards to interconnect telephone lines immediately followed the invention of the telephone. Local exchange networks developed rapidly in the United States, and the interconnection of local networks spread as quickly as advances in the art of transmission permitted. Exchanges in both New York and California opened early in 1878, following the installation of the first experimental switchboard in Boston the year before. Circuits were first placed in service between the east and west coasts in 1915.<sup>1</sup>

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<sup>1</sup> William B. Macurdy and Alistair S. Ritchie, *The Network: Forging Nationwide Telephone Links*, 53 Bell Lab. Records, No. 1 (January 1975), p. 6.

By 1925, trunk-switching tandem offices had come into being to interconnect local offices in areas, such as New York City, with dense telephone utilization. These offices were similar in design to local switching systems; and there was a natural tendency to extend the local tandem networks to serve shorthaul toll connections. Automatic alternate routing—the use of switching among alternate trunk groups when all the trunks in a direct group are busy—was not introduced until the early 1950's, in conjunction with direct distance dialing.

Toll service in the mid-1920's was accomplished by the use of direct intercity lines. Toll callers were requested to hang up, and their calls were queued until a circuit was free; then the calling party was contacted to complete the connection. Three to four operators were originally needed to complete the call through the distant local office to the called party. The switchboard and procedure were designed to make the most efficient use of costly toll circuits.

A landmark event occurred in 1925 with the combined line and recording method of toll handling, by which no more than one operator received the call from the customer, recorded charge details, and handled the connection. There were continual difficulties however, in connecting widely scattered points with traffic demand too light to justify the installation of direct lines. Calls between such areas required manual switching between two or more indirect or "short-distance" lines through intermediate offices, resulting in customer difficulty, substantial transmission losses, and delay in establishing the connection. During the 1930's the bulk of long-distance calls (e.g., 80 percent in 1936) were still handled by direct lines between cities in order to avoid service degradation associated with manual toll-board switching.

Nevertheless, it was evident by the late 1920's that a master plan was needed to systematically organize the telephone plant so as to limit as much as practicable the number of switches required for a toll connection, and to provide satisfactory transmission over any route. A.T. & T. announced a mandatory general toll switching plan in 1930. As gradually introduced during the next several years, the plan established a hierarchy of manual toll offices and an upgrading of some indirect toll lines to permit their switched interconnection to form long-distance circuits comparable to the then prevalent direct lines. The plan included direct lines wherever economically justified. The number of switched connections necessary to build a long-distance circuit was limited to a maximum of six, including the toll centers to which the local offices connected; and this required the introduction of costly wire and coaxial cable of higher transmission quality than other indirect toll lines. These were to interconnect the relatively inexpensive toll-board switches. These changes were the precursor to the installation of nationwide customer dialing in the postwar era, with its associated nationwide numbering plan, heavily utilized five-level hierarchy of switching offices, and automatic translation and routing features.

This evolving network constituted a stage of technological development that was implicitly obvious to the common carrier community in 1934. Hence, as the medium which provided telephone service, and as the aggregate of "lines" over which section 214 was to apply, this state-of-the-art was not documented and defined as a matter of record during the passage of the Communications Act. The effect of this



omission was for both the FCC and the Congress to attempt to define jurisdiction by later rulemaking and amendment. Technological advances were to make this task a difficult and controversial one, and jurisdiction was adopted over significant elements of transmission capacity and equipment in order to control the introduction of service and investment.

(b) *Early communications law.*—The expiration of the original Bell System patents in 1893 enabled independent entrepreneurs to construct and operate competing telephone companies and intercity lines. The Bell System companies attempted sporadically to purchase these competing exchanges, and it was not long before this practice became established policy. It aroused criticism from the independents, who felt that their existence was being threatened by monopoly. In most States, moreover, the granting of exclusive franchises was either unconstitutional or contrary to statutory law. Nonetheless, the issuance of competitive franchises was regularly followed by combination among franchisees, despite the efforts of legislatures to prevent it. The State utility service commissions created during the first decade of the century initially had very limited powers, although they extended their jurisdiction to telephone and telegraph companies as well as railroads.

Attempts to string parallel lines and to build duplicate facilities had come to be regarded as perverse and wasteful by the industry and a large segment of the public. Therefore, the emergence of the State commissions was the logical corollary to the development of the concept of "natural monopoly." This theory gradually appeared from the franchise experience to explain, on the one hand, the persistent tendency of direct, duplicative competition to produce inferior results and to disappear, and, on the other hand, to justify its abandonment.<sup>2</sup>

Regulation came about at a time when the voice network performed by means of wire-line cable systems associated with high capital costs and extensive rights-of-way. When one firm can supply the entire market at decreasing per-unit costs than several firms attempting to compete (for example, in communications), the "natural" result of market forces is the elimination of all firms but one. This is an all-embracing and traditional characteristic of natural monopoly, defined as economies of scale. The evolution of natural monopolies became the major rationalization of governmental restriction of entry.

Thus, State commissions throughout the country made the decision to supplant competition with active regulation. They typically refused to certify competing exchanges, and encouraged and endorsed mergers of existing companies. They also granted franchises to individual telephone companies to exclusively provide service within their operating territories.

The early State commissions were also empowered to prevent the competition that had been to some degree responsible for bringing about regulation in the first place. Most often, a carrier required a commission's "certificate of public convenience and necessity" prior to commencing "construction or operation of service or extension thereof."<sup>3</sup> This certification requirement was part of a general trend

<sup>2</sup> Kohn, *op. cit.*, II, n. 11, I, 118.

<sup>3</sup> *U.S. v. Amer. Tel. and Tel. Co., et al.*, "Defendants' First Statement and Contentions of Proof", Civil Action No. 74-1698 [D.C. Cir.], p. 104, citing 1927 *N.D. Sess. Laws* ch. 198 para. 1, etc.

of policy toward public utilities. Railroad companies were also made subject to the same requirement in State law and in the yet-to-be enacted Transportation Act, with the same controlling goals, that is, to prevent wasteful duplication and to protect existing lines from competition.

In return for these protective charters, the telephone companies were made subject to some form of rate regulation, and were made to assume the obligations of common carriers. The notion of common carrier is rooted in the common law duty to render adequate service at fair rates.<sup>4</sup> This obligation was codified and greatly expanded for the telephone industry to include the conception that the company has the general responsibility to extend supply as broadly as possible, and to continue to provide service even when it is uneconomical to do so. Thus, State law commonly empowered regulatory commissions to order a company "to extend its line, plant, or system into, and to render service to, a locality not already served when the existing public convenience and necessity require such extension and service," or to improve and maintain existing facilities. They also required commission approval of the "removal or discontinuance of any plant."<sup>5</sup> As was the requisite certification to establish a "service or extension thereof," these obligations preceded and were analogous to those passed into the Transportation Act and reenacted into the Communications Act of 1934.

In 1910, largely through agitation by the independents, the Federal Mann-Elkins Act extended the jurisdiction of the ICC to "wire or wireless" telephone, telegraph and cable companies.<sup>6</sup> There was some doubt, however, as to what classes of service and what companies were subject to the 1910 act. It was later revised somewhat through title IV of the Transportation Act of 1920. Very briefly, these amendments contained orders establishing standards for the provision of telecommunications services and facilities, for the establishment of charges by carriers, for investigations conducted by the Commission, and for the submission of reports.

In 1921, by amendment of the Transportation Act, the jurisdiction of the ICC over telephone companies was extended to consolidations and acquisitions of control. It was provided that once the Commission had issued a certificate approving a proposed consolidation, any act or acts of Congress which otherwise might make the action unlawful would not apply.<sup>7</sup> This amendment was explicitly for the purpose of allowing mergers of locally competing telephone exchanges, the legality of which might otherwise be questioned. This was an extension of existing State law and was not, as in the case of the railroad legislation enacted the year before, a systematic plan to directly bolster languishing returns of the affected companies. The 1920 language, as amended in the years 1920-21, was the basis for that enacted in title II of the Communications Act.<sup>8</sup>

<sup>4</sup> See, e.g., Warren A. Seavey, ed. *Cases of the Law of Public Utilities*, 2d ed. (St. Paul: West Publishing Co., 1936), pp. 1-6.

<sup>5</sup> *U.S. v. AT&T Co.*, op. cit. n. 3, p. 102, citing *Ore. Laws*, ch. 164, para. 2; *N.D. Sess. Laws*, ch. 209, para. 9.

<sup>6</sup> Act of June 18, 1910, ch. 309, Sect. 7, 36 Stat. 539 (Commerce Court Act).

<sup>7</sup> Act of June 10, 1921, ch. 20, 42 Stat. 27 (Willis-Graham Act).

<sup>8</sup> *A Bill to Regulate Interstate and Foreign Communications*, H.R. Rep. No. 1850, to accompany H.R. 8301, 73rd Cong., 2d Sess. (1934), pp. 5-7.

## *2. International common carrier*

Regulatory concern with international communications also had its beginning in the mid-nineteenth century. During the time period of 1857 to 1884, the landing of telegraph cables between the United States and foreign countries was, when needed, authorized by Congress. After 1879, in the absence of specific legislation, submarine cable landings were controlled by the Chief Executive. The authority given to the Interstate Commerce Commission over the transmitting of messages in foreign commerce applied only insofar as the transmission took place within the United States.<sup>9</sup> The President's right to issue cable landing licenses was codified in the Cable Landing License Act of 1921. By executive order, this authority was transferred to the Department of State (it was again delegated by the Eisenhower administration to the FCC through Executive Order No. 10530 in May, 1954, subject to the approval of the grant of landing licenses by the Secretary of State). There had been several telegraph cable carriers serving the U.S. mainland since the 1880's, both directly and through connecting carriers. These were Western Union Cables, Inc. (a subsidiary of Western Union Telegraph Co., which itself was organized in 1851), All America Cables, Inc. (operating principally between the United States and Latin America, and within Latin American countries: its corporate name was changed to All America Cables and Radio Inc. in 1938), and the Commercial Cable Co.

British companies already had been operating across the Atlantic for some years by 1881, the year that a cable laid between Nova Scotia and England was leased to the Western Union Telegraph Co. By the 1920s, a number of cables were laid between the North American and European continents. These major communications routes serving the industrialized nations were owned predominantly by the British; their companies had also pioneered in service in Latin American countries and across the Pacific. Throughout most of the world, then, cable landing sites existed at British naval stations and were connected to London. This British control continued through the first quarter of the twentieth century, when the newly developing radio medium decreased the importance of cables.<sup>10</sup>

After experiments with radio transmission at the turn of the century, the effort in the United States was to direct its use to areas that would not compete with the well-established cable industry. Radio-telegraph was capable of a function that cable couldn't provide—marine communications, particularly for safety of life at sea. Consequently, radio was confined primarily to ship-to-shore services extending over relatively short distances. The lack of effort expended to develop efficient transmitting and receiving equipment made transoceanic radio communication generally unsuccessful.

Just as early cable ownership was largely British, early radio operation between the United States and Europe, such as it was, was conducted by a British firm, established in 1895, the Marconi Wireless Telegraph Co., Ltd. In 1899, Marconi organized and retained control

<sup>9</sup> Act of Feb. 28, 1920, op. cit., II, n. 12, at 474, Sec. 400(1) (c).

<sup>10</sup> Asher H. Ende, *International Communications*, Federal Communications Bar Journal, vol. 28, nos. 2 & 3 (special combined issue, 1975), p. 149.



of a counterpart in the United States. However, with the advent of American participation in World War I, the U.S. Navy took control of all the Marconi Co.'s radio stations in the United States, as well as stations operated by French and German interests. Under the war-time controls, the Government combined the patent and scientific resources of all electrical manufacturers, resulting in the development of new means for satisfactory long-distance radio transmission and reception.

Following the war, the U.S. Government encouraged the consolidation of all these vital radio communication developments into one entity. Consequently, the Radio Corp. of America was formed in 1919. Its function was to handle international point-to-point radiotelegraph service from stations turned over to it by the Navy, after having purchased the assets of the British company. During its effort to break into a field dominated by cable, RCA recognized the competitive advantage of radio transmission due to the insensitivity of cost to distance. The cable companies had traditionally implemented their rates and charges to follow the cable routes, rather than a logical relationship to actual distance between points. Traffic was usually diverted from New York, for instance, through London to reach the Suez Canal area, and rates reflected this planning. RCA began to compete with the cable companies, with reduced rates not related to distance.

In 1920, RCA established radiotelegraph circuits between the United States and Great Britain, Hawaii, Japan, Norway, Germany, and France. A circuit to Italy was established in 1921, and to Poland in 1923. (As these services grew, RCA established two subsidiaries to conduct business that had previously been operated by company departments; they were Radiomarine Corp. of America, for service to and from ships, and RCA Communications, Inc. [RCAC, now RCA Global Communications, Inc.] for point-to-point service between stations.) This gave rise not only to intense competition between technologies, but also, as other radio companies entered the field, the worry that the old cable entities, threatened by the new mode, would attempt to control the radio companies to stifle competition.

The concern for preventing the "dead hand of the past," the cables, from controlling the future of radio was one impetus for the United States to enact regulatory legislation and to impose controls in the field.<sup>11</sup> A second concern during those very early years was to prevent monopoly and enhance competition in the manufacture of electronic equipment.<sup>12</sup> These two ideas grew out of the initial purpose of creating "order out of chaos."<sup>13</sup> The Interstate Commerce Commission had retained authority over domestic common carriers, but its limited power to regulate and license radio stations<sup>14</sup> had been abrogated by judicial decree.<sup>15</sup> Congress was obliged to reinstate and strengthen this power by creating the Federal Radio Commission.<sup>16</sup> Two provisions

<sup>11</sup> *Id.*, p. 151.

<sup>12</sup> RCA was apparently a main offender in this instance. See, generally, Report of the Federal Trade Commission on the Radio Industry to the House of Representatives, 67th Cong. 4th sess. (1923), chap. IV.

<sup>13</sup> *Ende*, op. cit., n. 10, p. 154.

<sup>14</sup> Act of Aug. 13, 1912, ch. 287, 37 Stat. 302 [Radio Act of 1912].

<sup>15</sup> See, e.g., *Hoover v. Inter-city Radio Co.*, 286 F. 1003 (1923).

<sup>16</sup> Act of Feb. 23, 1927, ch. 169, 44 Stat. 1162 [Radio Act of 1927]. See also discussion, *Telecommunications: Economics and Regulation*, Reprint ed. [New York: Arno Press Inc., 1974], ch. X.



were included in the Radio Act of 1927 to establish a procompetition policy in international communications. They were sections 15 and 17, which have been carried over as sections 313 and 314, respectively, of the Communications Act of 1934.<sup>17</sup>

Section 313, or the old section 15, was designed primarily to prevent monopolies in the manufacture of electrical or electronic equipment, and in interstate and foreign communications. By this provision the antitrust laws are made applicable to the manufacture and sale of radio apparatus and to radio communications under the agency's jurisdiction. Section 314, or the former section 17, addressed the need to separate cable from radio ownership and to insure that competition be maintained between cable and radio as two separate and distinct means of international communication. It prohibits ownership, control, and operation by any cable carrier of any radio entity engaged in interstate and foreign communications if the purpose or effect is to substantially lessen competition or to unlawfully create a monopoly. Entitled "Preservation of Competition in Commerce", section 314 became the converse of section 214 in title II, and the statutory basis for the FCC's authorization of competitive telegraph circuits. Substantive regulation in the international field, then, started with the Radio Act of 1927.

As is clear from a carefully worded statement of policy issued by the Federal Radio Commission, duplicating applications for entry were to be granted, when feasible:

The Commission, in making the foregoing decision, [issuance of construction permits and licenses for radiotelegraph service] adopted the following principle for its own guidance:

That competitive service be established where there are competing applications, or an application or applications to compete with the already established service, and that in the grant of competing licenses, fairness of competition be established, except that as to an isolated country, which, in the judgement of the Commission, will not afford sufficient business for competing wireless lines, only one grant of license shall be made, preferably the first application in priority.<sup>18</sup>

By this time, international point-to-point radio service seemed to have enormous business potential, and other companies began to move into the field shortly after RCA. For instance, by 1926, the Tropical Radio Telegraph Co. established 12 direct radiotelegraph circuits to the West Indies, Central America, and South America, and the International Telephone & Telegraph Co. organized Mackay Radio Co. in Delaware to challenge RCA's monopoly in worldwide radiotelegraph operations. By 1933, Mackay established circuits to countries in Europe and South America, and an associate, Mackay Radio & Telegraph Co. of California, provided transpacific service.<sup>19</sup> Government policy was to grant transoceanic frequencies only on a public utility basis, and not for private use.

<sup>17</sup> *Ende*, op. cit., n. 10, p. 155. See appendix (B) (2).

<sup>18</sup> Second Annual Report of the Federal Radio Commission to the Congress, 1928, p. 30.

<sup>19</sup> John M. Kittross, ed., *Documents in Telecommunications Policy*, Reprint ed. (New York: Arno Press, Inc., 1977), p. 132.

Although the technical capacity of radio transmission was initially limited to telegraph communication, experiments in the field of radiotelephony were begun by the U.S. Government in 1915. The first international radiotelephone circuit was established in 1927 between New York and London for general use. By the end of 1933, 10 direct radiotelephone circuits were established between North America and Western Europe; and in some cases line-wire connections were extended to countries beyond the distant radio circuit terminals. As the operations of the international record carriers evolved, A. T. & T. became the sole entity providing overseas message telephone service from the U.S. mainland.

The dicotomy of voice from record services between the United States and foreign points persists to this day, as an outgrowth of the historic distinction in the domestic sector. As do A. T. & T.'s and Western Union's domestic operations, the international record carriers derive their income from the rate of return they are allowed to earn on their rate base. The economic structure has been different, with regulation maintaining a monopoly for interstate service, and an oligopoly for delivery to overseas points. The international communications industry includes one dominant firm offering voice services, five providers of record services, and one technological monopolist (Comsat) which supplies satellite circuits (the dominant, present-day version of overseas radio) through a carriers' carrier arrangement with the other firms.

As a result, the Robert Dollar Steamship Co. organized Globe Wireless, Ltd., the United Fruit Co. created the Tropical Radio Telegraph Co. (now TRT Telecommunications Corp.), and the Firestone Tire & Rubber Co. created the United States-Liberia Radio Corp. to meet their special requirements. The facilities were made available to any customers.

Meanwhile, competition had been the rule in international cable transmission. France and Germany, as well as the United States, had observed the need to own and operate cable facilities to supplement those owned by England. Western Union Cables and the Commercial Cable Co. competed not only with each other, but also with foreign entities across the Atlantic. The distinction was maintained between the international record carriers using submarine telegraph cables and those using high frequency radio, to insure competition between the two means of transmission.

Nonetheless, as a result of the cost advantages and the tremendous marketing expansion of the radio medium, there were no major cable landings established after the mid-1920's, until the TAT series was begun in 1956. During this time, the operations of the cable carriers remained relatively static both in the United States and abroad.

#### *B. Section 214*

The legislative history of the Communications Act of 1934<sup>20</sup> indicates both a consensus that regulatory jurisdiction over the various facets of the communications field needed to be centralized, and a desire to harness the early monopolies. The Interstate Commerce Commission had dealt with the rates and practices of broadcasting and

<sup>20</sup> 47 U.S.C. 151 et seq.

common carrier companies in a number of cases, but its activities for the most part consisted of supervision over routine matters. The Commission had established no separate departments, bureaus, or divisions to deal exclusively with communications problems, the work being distributed throughout the organization as set up to supervise railroad policy. It was perceived in Congress that the agency lacked an effective legislative mandate to implement its mission. The Federal Radio Commission possessed the authority to oversee the operation, but not the rates and charges of radio companies. Jurisdiction over the granting of cable landing licenses resided in the executive branch, with the right to reserve and assign bands of radio frequencies to Government agencies; and this remained unaffected by the passage of the new act.

In the summer of 1933 the Secretary of Commerce appointed an interdepartmental committee on communications to consider a national communications policy. In its report the committee recommended that a Federal Communications Commission be established to centralize the jurisdiction of the Interstate Commerce Commission over wire and radio common carriers, of the Federal Radio Commission, and of the Postmaster General over telegraph companies and telegraph lines.<sup>21</sup>

In considering the bill sent to it from the Senate, the House committee had before it a comprehensive report on the subject of holding companies, authored by a consultant to supplement the proceedings of the interdepartmental committee. The "Splawn Report" presented statistics documenting the assets owned by companies in the various communications fields. It also reported the degree of concentration among domestic common carriers, and remarked on the relationship between facilities construction and the level of rates:

There is a higher degree of concentration of ownership of telephone facilities than of telegraph and cable facilities, as has been made apparent from the comparison of selected financial and operating statistics hereinafter set forth \* \* \*. The extent to which there is actual or potential competition between telephone companies may be observed when it is pointed out that the Bell System operates in all 48 States and the District of Columbia \* \* \* [in] 12 States and the District of Columbia \* \* \* the Bell System meets absolutely no competition from any other telephone company, unless it be such small companies as do not report to the Interstate Commerce Commission, and rural or farmer lines, for which no data were available \* \* \*.

Again, the competition which the Bell System meets may be determined from the fact that all companies other than those of the Bell System had gross revenues of only 5.72 percent of the total \* \* \*.

During the period 1922 to 1932, inclusive, American Telephone & Telegraph Co. made only four voluntary rate reductions in toll rates \* \* \*.

The holding company has been found as a result of this investigation to be as prolific of abuses in the field of communications as in other utilities already studied. What is dis-

<sup>21</sup> *Study of Communications by an Interdepartmental Committee* Report No. 1273, 73d Cong., 2d sess. (1934) (Roper Report).



closed by the examination of the Associated Telephone Utilities Co. is, in my judgment, but typical of what may occur under existing laws. Moreover, American Telephone & Telegraph Co., which is both a holding and an operating company, is more powerful and skilled than any State government with which it has to deal. A bill regulating communications in interstate commerce will fall far short of being effective unless it first restricts the use of the holding company to what is absolutely essential and necessary and second, unless the regulation is extended to the holding company in like manner as to the operating company.

The magnificent plant that the American Telephone & Telegraph Co. system owns has in the main been paid for by the users of the service. There is no difficulty about obtaining further capital for necessary expensions. The American people are entitled to know if they are being overcharged for this service.<sup>22</sup>

Both the House and Senate communications bills contained, with minor differences, an almost exact derivative of section I (18)-(22) of the Interstate Commerce Act.<sup>23</sup> In presenting the proposed legislation to the House, Sam Rayburn, chairman of the sponsoring committee, succinctly stated the source and purpose of section 214:

Section 214, relating to extensions of lines, is based upon section 1(18)-(22) of the Interstate Commerce Act, which relates only to transportation. It requires a certificate of public convenience and necessity from the Commission for the construction of a new interstate line but permits the construction of local lines without such certificate. The section is designed to prevent useless duplication of facilities, with consequent higher charges upon the users of the service.<sup>24</sup>

There was not a great deal of remark offered on the proposed section during hearing deliberations, although opinions were solicited intermittently. Conjecture as to its necessity was ambivalent:

The CHAIRMAN. Coming down to the meat of the proposal, which is to require a certificate of convenience and necessity for a new interstate telephone line \* \* \* what is your position on that?

Mr. GIFFORD. I think that in order to avoid duplicate plant in communication companies, I rather favor that, but how to do it and do it without time to study it that I think the new commission should have, I do not know. It is a very difficult thing to do, because it is like regulating the number of cars that should go on a train to take them on or off.

The CHAIRMAN. I am not at all certain that this provision ought to be in here \* \* \* But my point is this, laying all this aside, the question I would like to get an answer to is whether or not you think it is a desirable provision to prohibit or to require a certificate of convenience and necessity for interstate telephone line construction?

<sup>22</sup> *Preliminary Report on Communications Companies*, H. Rep. No. 273, 73d Cong., 2d Sess., pp. xii, xvii, xxx-xxxi (1934).

<sup>23</sup> See, for comparison of S. 2910 and H.R. 8301, *Communications Act of 1934, Conference Report*, Rep. No. 1918, 73d Cong., 2d Sess. (1934).

<sup>24</sup> 78 Cong. Rec. 10314 (1934).



Mr. GIFFORD. So far as the telephone business is concerned, I do not think it amounts to anything one way or the other, by working with the commission, if they want to take it up we can go over our projected program in advance and get together on some working basis.

The CHAIRMAN. I may say to you that there was some doubt as to the wisdom of it being put in here. We had to get the reaction to see what would happen.<sup>25</sup>

\* \* \* \* \*

The CHAIRMAN. Mr. Gifford, one of the very great reasons for that is just because nobody had control of the building of new lines, and a lot of improvident lines were built. Industries were built up along them, and now they are nothing but two streaks of rust, and the whole community has gone to the bad. \* \* \* I wanted to know what objection you have to authority being lodged in some administrative commission or power, to see to or approve the extension of lines, or new lines, in a field that is already served.

Mr. GIFFORD. I do not think that I have any objection, if it were worked out on a practical basis. This particular bill does not. I can see that it is not an easy thing to do.

The CHAIRMAN. What we are doing in this section is to give the power to approve, or veto, applications for extensions of new lines, or the building of new lines.

Mr. GIFFORD. But, we would have to submit every case to the Commission, I understand.

The CHAIRMAN. Yes; that is correct.

Mr. GIFFORD. And it runs into thousands almost every day.

The CHAIRMAN. You mean extensions of lines?

Mr. GIFFORD. Circuits, extensions of circuits.<sup>26</sup>

The CHAIRMAN. I am limiting myself to the extensions of existing lines, or building new lines. Do you think that that would be very serious?

Mr. GIFFORD. I do not think that that would be impossible.

The CHAIRMAN. Do you not think that there are a great many cases where it would have been a very fine thing and in the public interest to have had proper supervision as to the construction of some telephone lines. Do you not think that there have been a lot of improvident systems built that have cost some people a lot of money which they are going to lose?

Mr. GIFFORD. I do not think that they are in the telephone business, Mr. Chairman.

The CHAIRMAN. You do not?

<sup>25</sup> Testimony of Walter Gifford, president, AT&T Co., U.S. Senate, Committee on Interstate Commerce, *Hearings on S. 2910, Federal Communications Commission*, 73d Cong., 2d Sess., pp. 90-91 (1934).

<sup>26</sup> In the original drafts of S. 2910 and H.R. 8301, sec. 214 was entitled "Extension of Lines and Circuits", and required carriers to obtain certificates before they could extend, construct, acquire, or operate any line or circuit. The witness voiced a technical objection to the inclusion of telephone circuits in the requirements: "These provisions would prevent the placing of a new circuit on an existing pole line, although sudden changes in the demands for service frequently make it necessary to do such work, which could be done in a few days, if necessary, except for the securing of the permit. . . . This was incidental. I cannot believe it was meant. . . ." *Id.*, pp. 89-90. See discussion, *Mackay Radio and Telegraph Company*, Docket No. 4124, 6 FCC 562 (1938). Logically, the word was deleted "to meet a technical objection elaborated upon by a witness for the Bell System, so as to make it perfectly clear that there was no intention on the part of Congress to limit the right of carriers to make full use of their own physical facilities by the derivation of as many circuits as possible." at 573.

Mr. GIFFORD. No sir.

The CHAIRMAN. Well, you do not hear them all cry like I do.

Mr. GIFFORD. I beg your pardon.

The CHAIRMAN. I say, you do not hear them all cry like I do.

Mr. GIFFORD. I have heard no complaint.

The CHAIRMAN. I do not mean that all of them cry. I mean that those who do cry, come around here and tell their stories.<sup>27</sup>

A feeling existed during passage of the Communications Act that section 214 should explicitly prevent construction and extension into existing telephone exchange areas:

In connection with certificates of necessity and convenience, we think the provisions in section 214, for requiring such certificates are in substance wise and salutary provisions. The language of the bill, however, is perhaps broader than is or should be intended. We suggest one change in section 214(a) and one in section 214(e) as follows:

By adding after the \* \* \* word 'circuit' \* \* \* the words 'in the territory or to points or places not already served by such carrier with service of the same class.' \* \* \* And after the word 'any', the word 'such', so that it would then read:

Sec. 214(a) No carrier shall undertake extension of its line or circuit in the territory or to points or places not already served by such carrier with service of the same class, or shall require or operate any such line or circuit or extension thereof, or shall engage in transmission over or by means of such additional or extended line.<sup>28</sup>

\* \* \* \* \*

[S]ection 214 \* \* \* after the word 'circuit' add: 'If the territory through which a contemplated extended line or circuit is already, in part or in whole, occupied by another common carrier, the right of extension will not be granted without due notice to the carrier already occupying said territory and after due hearing by the Commission, and no common carrier subject to the provisions of this act shall invade or occupy the territory served by another carrier without due notice and a due and lawful hearing by the Commission \* \* \* and the Commission, if the territory is already occupied by another carrier, shall give due and timely notice to the end that the carrier already occupying said territory may appear and defend its right, if any, to continue to occupy said territory.'<sup>29</sup>

These proposals for protecting carrier territory were apparently not acted upon, since they or any like them were not contained in the section as enacted.<sup>30</sup>

<sup>27</sup> Testimony of Walter Gifford, president, A.T. & T., U.S. House, Committee on Interstate and Foreign Commerce, hearings on H.R. 8301, Federal Communications Commission, 73d Cong., 2d Sess., pp. 171-72 (1934).

<sup>28</sup> Testimony of R. B. White, president, Western Union Telegraph Co., U.S. Senate, op. cit., n. 25, pp. 104-05.

<sup>29</sup> Amendments proposed by the American Radio Audience League, U.S. Senate, id., pp. 114-15.

<sup>30</sup> Sec. 214 may have intended the Commission to prevent existing exchanges from being affected by certifications of carrier facilities, consistent with the intent of the original ICA clause and State regulation of local exchange telephone service. These market territories would be recognized by sec. 214 protection from incursion.

There were some reservations voiced, as well as some quite strenuous objections, to what was regarded as a direct and indiscriminate transfer of the provision intended for railroad regulation into a law devised for a largely unrelated industry:

Before considering the meaning of the provisions of this section as applied to the telephone business, I wish to make the general comment that there is no presumption in favor of the legislative method that has been followed in drafting this section. There is no reason to suppose that laws which are proper or necessary in connection with railroads are desirable or will work when applied to telephone systems. It has not been supposed heretofore that any sound conception of public policy required restrictions of this kind so far as telephone companies are concerned, and we do not know of any reason whatever why Congress should now, contrary to past experience, come to a different conclusion. Moreover, no one should be surprised if it appears from an examination of these provisions that they become impossible and absurd when the attempt is made to apply them to an entirely different business from that for which they were originally enacted.

Such a process of drafting important legislation is almost certain, it would seem to me, to lead to surprising and unintended results.<sup>31</sup>

\* \* \* \* \*

The CHAIRMAN. This principle for carriers is 14 years old, however. It is not something new. It was put into the Transportation Act of 1920.

Mr. GIFFORD. But it has never been applied to telephone companies.

The CHAIRMAN. Oh, no.

Mr. GIFFORD. And my point is that there is a big difference between a railroad track and a right-of-way, as a matter of fact, and the stringing of a couple of wires, or additional wires on a telephone pole.<sup>32</sup>

\* \* \* \* \*

[B]ecause the bill is so largely patterned after the Interstate Commerce Act, there should not be the same need for court test of its provisions as is usually true of new legislation. On the other hand, the mere fact that any unnecessary change has been made is apt to lead to a conclusion by the courts that a different construction of the new provision is intended. Mere rearrangement of existing provisions would not, of course, necessarily bring about that result, and generally little attention has been given to the order in which the provisions are set forth in the bill. But where there is any departure from the language of the acts which could open the doors to a different construction, our recommendations have been influenced by the thought that such possibility should not be permitted, unless clearly intended. Detailed consideration follows the arrangement of the bill.

<sup>31</sup> Testimony of Walter Gifford, U.S. Senate, op. cit., n. 25, p. 88.

<sup>32</sup> Testimony of Walter Gifford, U.S. House, op. cit., n. 27, p. 171.



Section 214: The provisions of section 1 (18)–(22) of the Interstate Commerce Act as to certificates of public convenience and necessity for rail construction are here adapted to construction of lines and circuits. Whether it is practicable or good policy to so extend these provisions, we do not undertake to say. Several provisions, however, undoubtedly will require further consideration.

It is assumed that the omission of the provisions relating to abandonment of lines is intentional.<sup>33</sup>

The words “line” and “circuit” are not defined. Perhaps they are self-sufficient, but any necessary definition should not be overlooked. A definition of “extension” also would seem desirable, so that the provisions would not hinder or preclude such necessary operating changes or rearrangements of existing lines or circuits for the purpose of meeting changes in the flow of traffic, which otherwise might technically be regarded as extensions of the prior separate lines or circuits.<sup>34</sup>

It was frequently observed that the amendment was ill-suited for the retention of competition between the telegraph carriers:

Section 214 of the bill is another section incorporating provisions of the interstate commerce laws which relate only to railroads without proper consideration of the differences requiring different treatment between the regulation of railroads, and the regulation of communications services. The provisions of section 214 \* \* \* are totally inappropriate in a bill which perpetuates, as this one does, the principle of competition between the telegraph companies, since these provisions could only result in weakening the competition of the smaller of the two competing telegraph companies.

In order that competition in this field may be continued in a healthy state, it is essential that each of the competing telegraph companies should be left in a position in which it is able to extend its lines and services freely and quickly, either by construction, by contract with the telephone company, with the independent telephone companies, with railroads or public utility companies, or by any other means. The proper conduct of a competing telegraph service frequently demands that the service be extended practically overnight into some new territory; and competition should not be hampered by the enactment of provisions such as those contained in section 214, unless it is determined to do away with competition between the two telegraph companies by permitting their consolidation subject to adequate safeguards.

There is no such public interest in limiting the extension of telegraph facilities as there is in limiting the extension of railroad tracks. Such extensions create no additional problems of highway transportation or additional dangers to the public, as in the case of railroad extensions.

<sup>33</sup> See p. 33 for more discussion of the abandonment clause.

<sup>34</sup> Supplementary Report of the Interstate Commerce Commission, U.S. Senate, *op. cit.*, n. 25, pp. 200–01, U.S. House, n. 27, pp. 88–89.

In any bill which perpetuates the principle of competition in the telegraph field, the provisions of section 214 should be wholly eliminated.<sup>35</sup>

The domestic telegraph systems to which the recommendation refers are the Western Union Telegraph Co. and the Postal Telegraph & Cable Co. The FCC did subsequently recommend an antitrust exemption in a new section 222 to permit consolidations and mergers of domestic telegraph carriers, subject to agency approval. This was one of a number of proposals submitted by the Commission pursuant to the directive in section 4(k) of the act that it "make a special report not later than February 1, 1935, recommending such amendments to this act as it deems desirable in the public interest." (This clause was deleted by the Communications Act Amendments of 1952.)

It is notable that, as enacted, section 214(d) was the same language as that contained in section I(21) of the railroad legislation, undoubtedly carrying with it the due process obligations enunciated some years before in *ICC v. Oregon-Washington Railroad & Navigation Co.*<sup>36</sup>

A quite conservative element is evident from the facts that the telegraph consolidation issue was left in abeyance by the 73d Congress, and that the language in title II and so much else in the bill was adapted basically from transportation law as well as a preliminary, hardly improved upon communications common carrier statute. The 73d Congress was hardly as willing to explore new theory of regulation as had been the members of the 1920 Congress. The announcement by President Roosevelt of his support for a "single Government agency charged with broad authority" was for the purpose of little more than "for the sake of clarity and effectiveness" in the relationship of the Federal Government to the public utilities.<sup>37</sup> Nor did there exist, as in the 19th century, a vocal public temper provoked by extortionate corporate practice. The commentary of the day,

<sup>35</sup> Supplementary Memorandum on Behalf of International Telephone & Telegraph Co., et al., U.S. House, id., p. 229.

<sup>36</sup> It seems that sec. 214(d) was supplemented by such legislation as the 1949 amendments to the Rural Electrification Act of 1936 (Act of Oct. 23, 1949, ch. 776, sec. 2, 63 Stat. 948) authorizing the Rural Electrification Administration to make loans for the expansion and improvement of rural telephone service. The House Committee on Agriculture, in recommending a bill for this purpose, stated that the ratio of telephones to number of residents in rural areas was as little as about one-tenth of the urban ratio. Rural Telephone Service, report to accompany H.R. 2960, H.R. Report No. 246, 81st Cong., 1st sess. (1949), p. 6. It was apparent that of the many thousands of mutual and farmer-owned lines and systems that had operated in the nonservice areas, many had been combined with independent and Bell carriers extending service from nearby city exchanges. Id. The committee reviewed a telephone company policy that effectively denied service to areas with relatively sparse population density:

Although they claimed to favor the area service type of development, witnesses for the telephone industry, both independents and Bell system operators, almost unanimously refused to commit themselves to provide area service in the areas in which they operate and over which they have in most cases a monopoly. There is every indication that unless they are forced to take such action, they will continue their policy of "skimming the cream" of the telephone business running their lines down the highways into the most profitable areas and relegating farmers in the less profitable service areas perpetually to a nontelephone hinterland. Id., p. 8.

Without in any way elaborating on the due process implications of "forc[ing] the telephone companies] to take such action," the committee felt that "[t]his bill, while giving every protection and preference to existing telephone companies, establishes the policy of area service as one of the criteria on which the Administrator will base his decision in granting applications for loans." Id., p. 9. By inference, the 81st Congress established a loan mechanism policy to provide and maintain an essential public utility service, as a preference to a commission-instituted and undoubtedly extensive hearing and compensation process which would have been necessary to satisfy the fifth amendment requirements of *ICC v. Washington-Oregon R. Co.*

<sup>37</sup> Message to Congress, Feb. 26, 1934, reprinted in *Regulation of Interstate and Foreign Communications by Wire and Radio*, H.R. Rept. No. 1850, 73d Cong., 2d sess., p. 1 (1934).

and the talent and resources, were undoubtedly more occupied with critical economic havoc caused by the depression. The President did advise that the new commission be given, in addition to the powers transferred to it from other agencies, "full power to investigate and study the business of existing companies and make recommendations to the Congress for additional legislation at the next session,"<sup>38</sup> but did not recommend that its powers be broadened or extended at that time.

The House committee that reported the bill remarked that the Interstate Commerce Act, as amended in 1910 to apply to communications, had never been perfected to encompass adequate oversight of the industry, but was really an adaptation from railroad regulation. Consequently, the intent of its bill was to account for the "many inconsistencies in terms of the act and [the] many important gaps which hinder effective regulation."<sup>39</sup> However, there existed both here and in the Senate committee a basic acquiescence to the adaptation of the intent of railroad law to the communications field:

In this bill the attempt has been made to preserve the value of court and commission interpretation of [the Interstate Commerce Act], but at the same time modifying the provision so as to provide adequately for the regulation of communication common carriers.<sup>40</sup>

[V]ariations or departures from the text of the Interstate Commerce Act are made for the purpose of clarification in their application to communications, rather than as a modification of congressional intent to attain a different objective.<sup>41</sup>

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<sup>38</sup> *Id.*, p. 2.

<sup>39</sup> *Id.*, p. 4.

<sup>40</sup> *Loc. cit.*

<sup>41</sup> Senate Rept. No. 781, 73d Cong., 2d Sess. (1934), p. 2.



#### IV. THE FORMATION OF POLICY

##### A. The Congress

The only significant legislative attention to section 214 occurred in 1943 during the passage of section 222. The new legislation was needed to relieve the economic effects brought on by the inadequacy of demand for telegraph service from more than one enterprise. The telegraph industry's financial trouble had its basis mainly in the depression, facilities duplication, and the growing ascendancy of voice telephone service. Section 222 also imposed requirements for a traffic routing formula in an attempt to maintain relatively fixed market shares and thus discourage aggressive competition among the international record carriers.<sup>1</sup>

Section 214(a)-(d) was amended to make "certain technical clarifying changes in the present act to conform with the merger legislation."<sup>2</sup> A requirement was imposed in section 214(a) that a certificate must be obtained to "discontinue, reduce, or impair service to a community or part of a community."<sup>3</sup> It is noteworthy that there is no documentation that indicates specifically why the "abandonments" language was deleted in its conversion to the 1934 act. At any rate, the essential clause was made more definitive and reinstated to anticipate the objection that a consolidated company would not develop and maintain service to the degree that might occur under competitive conditions.<sup>4</sup> The use of the term "service" in the amendment did not evidence a congressional intent to provide a loophole for facilities abandonment, as has sometimes been believed. The language was preferable to the House version of the clause, prohibiting the abandonment without Commission approval, of a "line, plant, office, or other physical facility." It was felt that this more explicit syntax might allow the abandonment of equipment which, though remote, could be critical to the operation of a line and hence of the maintenance of service. The broad term "service" was meant also to be a standard for evaluating whether the abandonment of a "line" was significant enough to warrant prior approval. It was to prevent an inadvertent requirement that the carriers file "literally thousands of applications for what are, in effect, minor installations or abandonments."<sup>5</sup>

<sup>1</sup> For a complete explanation of the sec. 222 provisions, refer to the report of the Federal Communications Commission, *An Overview of International Telecommunications: Industry Structure and Commission Policies*, Mar. 23, 1977, U.S. House, Committee on Interstate and Foreign Commerce, Hearings on International Communications Service, 95th Cong., 1st Sess., pp. 473-75.

<sup>2</sup> 89 Cong. Rec. 340 (1943).

<sup>3</sup> See Appendix B(3).

<sup>4</sup> It is interesting that, during debate on the 1943 amendments, there was discussed a suspicion of an "agreement, possibly collusion, between the telegraph companies and the telephone companies to the effect that the telegraph would abandon offices because they could save clerk hire and increase the telephone business by requiring the person sending the telegram to telephone [to] the point where a telegraph office was maintained." (89 Cong. Rec. 787). There is no other evidence that this allegation was in mind during drafting and approval of the abandonments amendment.

<sup>5</sup> Remarks of Mr. McFarland, 89 Cong., Rec. 1093 (1943).

The abandonments amendment also accommodated the high-priority war effort. The term "community" was broad enough, it was believed, to prevent the discontinuance of service to a military establishment or a war production plant.<sup>6</sup>

Section 214(a) was further refined to include a definition of the word "line."<sup>7</sup> The Communications Act had not previously included such a definition; both the Commission and A.T. & T. took the opportunity to obtain an understandable interpretation of the term. A.T. & T. asked for a definition which would have limited the term to conductors—that is, pole lines, wires, or cable. The Commission supported an interpretation meaning "any channel of communication," and it was this definition that was added to section 214(d) :

The tremendous scientific advance in communications has outmoded the old belief that a line is a copper wire strung on poles. Modern scientific development has made it possible by the installation of such gadgets as "phantom circuits" and "repeater coils" to carry on as many as 244 simultaneous conversations on a single pair of wires. As a result, carriers have felt that they have been unduly burdened by having to file applications \* \* \* in which major installations \* \* \* were not at issue. This has added to the book and paper work of the Communications Commission and of the carriers. The definition of "line" \* \* \* conforms in substantial degree with the definition heretofore exercised by the Commission.<sup>8</sup>

The definition was meant also to supplement the term "service" in the discontinuance provision so as to make it "extend over a much wider field technically and practically."<sup>9</sup> The proviso clause that accompanied the definition was the main vehicle for removing paper-work requirements for inconsequential facility changes.

Finally, the language in section 214(d) was adjusted to conform with 214(a) as part of the effort to insure that no "community" would be deprived, as a result of merger, of "any element of service."<sup>10</sup> In this case, after merger, one or two existing offices in the same town must still be maintained, and "under the very language of the bill, a community can get service if it is entitled to it."<sup>11</sup>

### *B. The Commission*

Beginning shortly after the enactment of the Communications Act, there was considerable confusion surrounding section 214 applications due to the dearth of statutory explanation of the term "line" and hence of the Congressional intent for actual administration of the approval or denial of extensions. Consequently, the first applications filed by the Bell System companies were quite inclusive and were examined thoroughly by the FCC staff, particularly as to questions of engineering justification and accounting impact. The interpretation put forth by the Commission law department was apparently very broad. However, by the time, in the latter part of the decade, that the Commission began

<sup>6</sup> Consolidation and Mergers of Domestic Telegraph Carriers, H.R. Rept. No. 69, 78th Cong., 1st sess. (1943), p. 10.

<sup>7</sup> See appendix B(3).

<sup>8</sup> Remarks of Senator McFarland, 89 Cong., Rec. 1093 (1943).

<sup>9</sup> Remarks of Senator Wadsworth, 89 Cong. Rec. 777 (1943).

<sup>10</sup> Remarks of Senator McFarland, 89 Cong. Rec. 1093 (1943).

<sup>11</sup> Remarks of Senator Wadsworth, 89 Cong. Rec. 787 (1943). See appendix B(3).



to issue its significant rulemakings on the issue, the domestic carriers had apparently decided that section 214 required applications only for the construction of physical pole lines whose terminals were located in different States. "Authorizations in the international sector did not devolve on explicit problems of definition. While the statutory mechanism was not the same, section 214 standards were utilized here early in the FCC's career and were judicially affirmed. There was no concern expressed about control of facility investments as a matter of section 314 regulation in the international sector. Route mileage does not affect cost increments in the radio mode; and capital investment was mostly a function of the establishment of transmitting stations pursuant to construction permits issued prior to licensing. What follows is an introductory review of the Commission's initial formulation of controlling certification goals in the domestic and international sectors, proceeding a detailed analysis in casebook fashion.

The proceeding in *Mackay Radio and Telegraph Co.* was the first formal Commission attempt to adjudicate the purpose of section 214. A determination of the term "line" was pivotal to the outcome since that established the reach of the statute for the purpose of regulating competitive service offerings. It was companion to *Southwestern Bell Telephone Co.*, which determined the effect of new additions to intrastate facilities. As will be seen, the test for facilities requiring authorization was whether or not they were intended to provide interstate "channels of communication." The Commission expanded the application of the term "line" in the "phantom circuits" case—*American Telephone and Telegraph Co.*—to insure that carriers would not misinterpret their certification responsibilities while installing newly-developed and capital-intensive rate base acquisitions.

Several other proceedings involving both Mackay Radio and RCA Communications illustrate how the Commission came to apply certification to extensions of service in the international communications industry. As has been seen, the services under discussion required title III rulings for radio licensing rather than section 214 certification; and they inherited a strongly competitive mandate from the Radio Act. However, the FCC denied Mackay's request in the initial case, holding itself to an examination of the "public interest" impacts of entry. The Court of Appeals subsequently affirmed the FCC's denial after indirectly examining the purpose of section 214 through reference to that of 1(18)–(22) of the Interstate Commerce Act. The war years saw a procedure of allowing duplication for national security purposes, and shortly afterward, while ruling on the "Bermuda Circuits" proceeding, the FCC made a distinct preference for this policy reversal. As related in the text of that decision, however, this inclination was frustrated by a "single circuit" agreement entered into with the British Commonwealth. Later, in the 1951 decision of *Mackay Radio and Telegraph Co.*, the Commission attempted to make assignments to Mackay in order to conform with what was seen as a "national policy" of competition. On remand from the Supreme Court, the agency was obliged to refine and justify its ruling. Although the FCC was now loathe to articulate general policy on the matter one way or the other, it did, from then on, make grants of duplicative direct circuits in radiotelegraphy.



### 1. Domestic common carrier

(a) *Mackay Radio and Telegraph Co., Inc.*, 6 FCC 562 (1938).—The facts of the *Mackay* case are as follows: In March 1936, RCA Communications, Inc., received a certificate of public convenience and necessity from the FCC to acquire and operate a two-way telegraph circuit between New York, Washington, and Baltimore. The circuit was to be leased from Western Union Telegraph Co. as specified in the application submitted by RCA.

In June 1936, Mackay leased from Postal Telegraph Cable Co. (both associates of the International Telephone & Telegraph System) a similar facility between Washington and Baltimore. In so doing, Mackay was competing with RCA, and it had never applied for or received a section 214 certificate. The circuit leased by Mackay was not permanently confined to any particular Postal circuit or wire; the arrangement required no new physical construction or capital outlay. Mackay's practice of transferring its circuit from one part of Postal's facility to another was similar to that followed by other carriers:

The Mackay Radio System is constantly utilizing circuits derived from Postal's existing plant, and numerous interchanges are made from time to time of the use of circuits between Western Union and Postal on the one hand and the Bell System companies on the other. These interchanges are of various types and are often required to be made upon an hour's or even a few minutes' notice in order to meet the exigencies of the service, but always involve the utilization of circuits derived from existing plant. In the Bell System additional circuits are procured from existing plant in two ways, (1) from existing facilities owned by the company in question, and (2) from existing facilities owned by other companies, such other companies being either Bell or independently owned.<sup>12</sup>

In September 1936, the Commission instituted a notice of inquiry to determine whether a telegraph carrier needed a section 214 certificate to extend service to a new territory through lease of wire telegraph circuits. The proceeding was also to consider whether additional rules were needed to implement section 214.

In the context of this question of entry regulation, the actual issue on which testimony was received was whether, as argued by Mackay and supported by Postal and A.T. & T., the term "line" was limited to the acquisition of physical wire to supplement interstate pole lines. The decision cited *Transit Comm. v. U.S.*<sup>13</sup> and extensively reviewed the legislative history of section 214.

The Commission found that section 214 applied to the acquisition of circuits through lease for the extension of telegraph service, regardless of whether interchange facilities were needed to extend the service to a new point of communication or whether the lease provided for the exclusive use of the lessor's physical facilities.<sup>14</sup>

<sup>12</sup> *Mackay Radio*, at 565.

<sup>13</sup> 289 U.S. 121 (1932). The Supreme Court interpreted the intent of sec. I(18) of the ICA by holding that a railroad operation over tracks leased from another carrier was an "extension" for which a certificate was required. The FCC regarded this case as analogous to Mackay's lease arrangement with Postal.

<sup>14</sup> *Mackay Radio*, at 569.

In discussing the deletion of the word "circuit" from the original draft of section 214, the Commission continued:

It is our opinion that the deletion referred to was merely to meet a technical objection \* \* \* so as to make it perfectly clear that there was no intention on the part of Congress to limit the right of carriers to make full use of their own physical facilities by the derivation of as many circuits thereon or therefrom as might be possible. Therefore, it is not our opinion that section 214 requires a certificate of public convenience and necessity when a company of the Bell System rearranges its circuits or derives new circuits so as to make maximum use of its facilities, when the result is not an extension of a particular company's service into fields not theretofore served by it. Nor are the provisions of this section necessarily invoked every time one of these companies enters into a different contractual arrangement in order to more effectively serve an area already served by it by some other arrangement. It is thought that the discussions that took place in the course of the passage of the Communications Act indicate a congressional purpose to give the Commission considerable latitude to interpret and administer this section in such a manner as not to obstruct the fullest development of efficiency of operation of the various companies in the territory or area served by them.<sup>15</sup>

Mackay contended that it acquired a wire circuit, which functioned merely as an electrical path for the transmission of impulses; and that since this did not entail construction, section 214 did not apply to the lease arrangement. It is clear, however, that the FCC was concerned with its ability to control competition brought about through any "acquisition," "operation," or transmission "over or by means of" additional or extended lines. Section 214 contained these terms, in addition to its application to "construction"; and they enhanced the Commission's ability to determine whether competitive entry would be in the public interest.<sup>16</sup>

With regard to the intent of section 214 for conditions of duplication and competition, the Commission explicitly held itself to interpretations construed under the ICA:

[We conclude] that the twofold purpose of the corresponding provision of the Interstate Commerce Act is definitely involved in section 214 of the Communications Act: to wit: (1) To prevent a carrier from weakening itself by constructing or acquiring or operating superfluous lines, and (2) to protect a carrier from being weakened by another carrier operating a competing line not required in the public interest.<sup>17</sup>

Thus, the *Mackay* case clearly rejected limiting section 214 to the construction of physical wire lines, and that carrier was directed to submit an application to lease the circuit. In order to prevent destruc-

<sup>15</sup> *Id.*, at 573.

<sup>16</sup> *Id.*, at 573-74.

<sup>17</sup> *Id.*, at 576-77.



tive carrier competition, the Commission construed the term "line" to encompass the communication service to be rendered over a "line," the circuits necessary for such service, and, by implication, the physical facilities required for, or incidental to, such operation. Exempted were only the rearrangements of circuits so as to make maximum use of authorized existing facilities to render authorized service to points of communication.

Impliedly also, the installation of new switches is accomplished in part through the exempted action of "when a company of the Bell System rearranges its circuits or derives new circuits so as to make maximum use of its facilities \* \* \*". Switches are also arguably involved when circuits are attained through partial lease or by the use of "numerous interchanges" to derive the various actual circuits which made up the "circuit" leased to Mackay. Likely because toll-board switches constituted a relatively minor segment of the interstate transmission function at that time, the Commission did not discuss the effect of switching, and evidently did not perceive the question of jurisdiction over these discrete facilities. This relegation of the switching issue occurs also in the *Southwestern* case, concluded the same day, though the function of toll switching created an additional jurisdiction controversy. It is notable, too, that the Commission did not promulgate rules which might have clarified the application of section 214 then and now.

(b) *Southwestern Bell Telephone Co., 6 FCC 529 (1938)*.—The factual situation in *Southwestern* is as follows: A.T. & T. applied for certification to supplement its existing facilities between Dallas and San Antonio. It requested authority to string an additional pair of wires (with mention of associated switching equipment) upon existing pole equipment owned by Southwestern Bell. The construction was to be performed by Southwestern in conjunction with its expansion of intrastate toll facilities along the same routes. Southwestern's facilities were to terminate at switchboards located within the State of Texas, but 10 percent of the traffic was estimated to be interstate, directed through switching connections effected from time to time at those switchboards.

The Commission granted the A.T. & T. application, but directed the companies to file a statement to support their contention that the Southwestern Bell facilities did not require a section 214 application and certificate. The National Association of Railroad and Utilities Commissioners (NARUC) was also granted leave to intervene and file a statement.

A.T. & T. conceded that its new facilities constituted part of its interstate system. However, the carriers argued in favor of the "physical line plant" theory, that the terminal apparatus must be located in separate States, and that physical construction must extend across State lines before jurisdiction may be invoked. Any interstate transmission conducted through the switching function could not be responsible to Federal authority, it was argued, as that would invade State jurisdiction.

The decision noted that it was not denied that proposed facilities were to be part of Southwestern Bell's interstate system, and were not to be discrete from its interstate facilities. It reviewed railroad cases in which the Supreme Court had rejected the exception provided in



1(18)—“spur, industrial, train, switching or side tracks located wholly within one State”—when the otherwise excepted tracks carried interstate traffic. The Commission extended this logic by stating that “preponderance of use” could be no test for the determination of jurisdiction:

We find no authority for the theory advanced by the telephone companies to the effect that this Commission should regard its jurisdiction with respect to the construction of a new line or the extension of any line as being limited to such toll facilities as are intended to be used “primarily” for interstate service. Congress provided no such test. It could have done so if it had so desired. Quite probably, one reason for the absence from the act itself of such a test is that it would be no test. It is doubtful whether the companies themselves, or the Commission, can arbitrarily fix a line to distinguish between that service which is “primary” and that which is “secondary” or “incidental.”<sup>18</sup>

This reasoning apparently expedited the Commission’s responsibilities in other areas. A crucial example was its discretion to assign all associated facilities to the interstate jurisdiction, including the re-routing operation of switching:

If companies themselves have the discretion to determine, for the purposes of section 214(a) of the act, whether new facilities, admittedly used in some degree for interstate transmission of messages, are or are not interstate facilities, it will be difficult and embarrassing, if not impossible, for the Commission to exercise the power expressly given to it by Section 221(c) of the act to classify the property of telephone companies ‘and determine what property of said carrier shall be considered as used in interstate or foreign telephone toll service.’ In view of the latter section we cannot attribute to Congress an intent to leave with the carrier the discretion to determine the corresponding question involved in the administration of section 214(a) of the act, and to base that determination on whether or not interstate use is made possible by operation of a switch or similar device.<sup>19</sup>

The carriers were advisedly to interpret this decision in conjunction with *Mackay Radio*:

As to the so-called ‘physical line plant’ theory advanced in the brief filed by the telephone companies, according to which it is contended that actual physical construction must extend across State line before section 214 of the act may be

<sup>18</sup> *Southwestern Bell*, at 532.

<sup>19</sup> *Id.*, at 533.

In 1938, sec. 221(c) was the legislative authority for the FCC’s role in the separations process. As now, with the cooperation of the industry, it devised the interstate rate base as a separate and distinct entity from the intrastate counterpart. In that year, however, the “board-to-board” method of ratemaking was in effect, i.e., none of the joint costs of the local telephone exchange were assigned to the interstate jurisdiction. The “station-to-station” method was introduced in 1943, as a response to the 1930 decision in *Smith v. Illinois Bell Tel. Co.* 282 U.S. 133. Station-to-station ratemaking recognizes the role of the local exchange in interstate service by allocating a portion of its facilities costs to the interstate rate base, in accordance with its “relative use” for interstate service. The FCC did not gain, however, any jurisdiction over facilities planned strictly for the local exchange.

invoked, reference is made to the case of *Transit Commission v. United States*, 289 U.S. 121, and to our decision of this date in the matter of Mackay Radio & Telegraph Co.'s acquisition and operation of a line or circuit extending from Washington, D.C., to Baltimore, Maryland (docket No. 4124). Without repeating what we said in that case, we reaffirm the interpretation placed upon section 214 of the act in that decision.<sup>20</sup>

*Southwestern Bell* appears to have been a major and logical extension of *Mackay's* policy toward leasing of circuits. By this action, and by the rejection of the use of switching to artificially predetermine interstate transmission, the "physical line plant" theory was effectively buried. The Commission exerted itself to undisputedly fix its authority over all interstate toll lines provided by the regulated monopoly, whether or not those lines also provide intrastate capacity.

The issues in *Mackay Radio* and *Southwestern Bell* were consciously selected and decided the same day in order to test and settle the FCC's case toward the two sides of section 214's "coin": the control of competition and the control of additions to the interstate rate base. The regulatory goal in *Southwestern* was not, as in *Mackay*, to restrain competition, for no competition to A.T. & T.'s interstate message telephone service existed. Rather, it was to control the entry of facility investment into the interstate rate base. It also determined that section 214's "line" was clearly an interstate circuit or an interstate channel of communication for purposes of establishing which services (as in *Mackay*) and which facilities (as in *Southwestern*) required prior authorization. It was this interpretation that was added to section 214(a) in 1943, in preference to the position of the carriers that the meaning given to the term should be a wire or, at most, a system of wires connecting telephone or telegraph stations with one another.

As in *Mackay Radio*, the Commission did not explicitly assert jurisdiction over switching facilities necessary for interstate transmission. The effect of switching was established, and was more obvious than in *Mackay*; but the status of interstate switches was not discussed. Both cases, however, were brought to hearing and resolved during a time when, unlike now, the switching function was a relatively minor and inexpensive portion of A.T. & T.'s overall effort to build and refine a toll network that could provide expedient, sound connections between telephones. As will be discussed,<sup>21</sup> that system is the basis of the sophisticated and completely integrated function that the present-day five-level switching system provides in rendering service. In contrast, and as background of the 1943 amendments, the so-called "Phantom Circuits" case established explicit section 214 rate base control over other elements of cost, such as carrier and multiplex equipment.

(c) *American Telephone & Telegraph Co., 10 FCC 315 (1944)*.—The Commission initiated this proceeding in 1942 in order to examine the facts involved in the establishment by A.T. & T. and the New York Telephone Co., of carrier systems on existing conductors between New York City and Boston. The questions at issue were whether carrier systems constituted "lines" as defined in section 214(a), and whether

<sup>20</sup> Id., at 534.

<sup>21</sup> See below, pp. 52-79.



the steps taken in building carrier systems constituted "new construction" within the meaning of the proviso clause in section 214(a).

Carrier systems were regarded as an alternative and cheaper method to the installation of additional voice frequency cables to add needed capacity. In essence, the parallel channels dedicated to each distinct two-way communications path were modulated and interconnected so as to derive more circuits per pair of wires than was feasible with voice frequency operation. Capacity was obtained for many more simultaneous conversations from a pair of wires which was otherwise capable of transmitting only one conversation. The extent of carrier use in the Bell System represented approximately 19 percent of long distance circuit mileage by 1942. A.T. & T.'s action was selected by the Commission as representative of the factors pertinent to the settling of section 214 policy toward the construction and operation of such equipment.

The decision found that the new capacity provided by the project constituted additional "lines" under the 1943 amendments, and that its installation did entail "new construction." The carriers were held to the requirements of section 214 through a review of this logic and of the Commission's own statutory responsibilities:

There can be no doubt that the carrier system provided over the New York-Boston route resulted in new channels of communication established by the use of appropriate equipment. Respondents themselves explicitly recognized that each carrier system between New York and Boston produced 12 new "circuits" or "channels," taking this position in the proceeding herein prior to the time that Congress defined "line" as meaning "any channel of communication." It is also clear that the channels of communication produced by carrier systems are not established by the "interconnection of two or more existing channels." When channels are produced by the interconnection of existing channels, a longer channel may result, but the number of channels at any cross section of the route is not increased. In the situation developed in this proceeding, however, the number of channels at any cross section of the route was substantially increased. Ninety-six channels were derived from sixteen pairs of wires, producing channels which had not previously existed. This result was achieved not by interconnecting existing channels, but by the removal of equipment used in voice frequency operation and the incorporation into the cable system between New York City and Boston of a substantial amount of appropriate carrier equipment. We find and conclude that the channels of communication produced by the use of carrier equipment constitute "lines" within the meaning of section 214(a) of the Communications Act of 1934, as amended.

Under our previous findings, authorization should be obtained from the Commission before additional channels of interstate communication are established by means of carrier systems, provided that the establishment of these additional channels constitutes "new construction" within the meaning of the last proviso clause of section 214(a) of the Act. \* \* \* The establishment of carrier systems over the New York-Boston route, which we consider as typical of other carrier



systems, required a substantial amount of construction in providing new wire lengths, buildings and other structures, and involved extensive construction work in removing voice frequency equipment and providing carrier equipment. We find and conclude that the changes in plant and equipment involved in providing carrier systems constitute "new construction" within the meaning of the last proviso clause of section 214(a).

It follows from the foregoing that the requirements of section 214 with respect to the obtaining of prior authorization apply to the construction and operation of carrier systems. This is in keeping with the purposes of that section as related to the increasing importance of carrier systems as a method of providing channels of interstate communication. One of the purposes of section 214 is to prevent improvident increases in facilities, with consequent higher charges to the users of the service \* \* \*. It would be anomalous to exclude from the scope of section 214 a method of providing communication channels as significant as the carrier method and to interpret such section as limited to the provision of new channels by means of additional wires.<sup>22</sup>

The reach of section 214 was significantly broadened in this instance to a broad range of "appropriate equipment" necessary for service involving new construction. While absolute certainty would necessitate a thorough legislative history of the 1943 amendments, it seems that the policy established in "Phantom Circuits" did not contravene the intent of Congress in 1943. Evidently, that Congress did not intend to release the carriers from section 214 responsibility to any significant extent; its amendment was ancillary to the primary legislative purpose of permitting the merger of domestic telegraph companies.

The overall accomplishment of these three landmark rulemakings—*Mackay Radio*, *Southwestern Bell*, and "Phantom Circuits"—was to establish the section 214 requirement over any form of communications technology which derives channels in interstate service. It is obvious that the Commission was loathe to limit its jurisdiction. This might have been due less to "creeping federalism" than to the fact that communications technology was starting to become, very soon after the passage of the 1934 act, much more convoluted than the railroad track, lines, and switching mechanisms to which its predecessor legislation applied.

Furthermore, section 214 is almost completely devoid of any standards as to apparatus classification, market and service definition, and relevant conditions on certification grants. In fact, a case could be made that section 214 is actually an undefined, administrative title in itself, separate and distinct from the reporting and ratemaking specifications in the rest of title II. When it is recalled that one of its two main intends is to control competition and insure satisfactory service—an entry and exit control function—this point could be illustrated by reference to the radio services title.

Each clause of title III is in some way related to the conditional and procedural stipulations involved in grants, revocations, and modifica-

<sup>22</sup> *American Telephone & Telegraph Co.*, at 319-20.

tions of radio construction permits and operating licenses. No station can exist without having been called to account for the issuance of a "certificate." Yet neither the Congress nor the Commission itself took the opportunity to designate, in any appreciable fashion, the indexes to the FCC's "licensing" power over the provision of new carrier facilities and services.

## *2. International common carrier*

(a) *Mackay Radio & Telegraph Co., Inc.*, 2 FCC 592 (1936); *aff'd.*, 68 App. D.C. 336 (D.C. Cir., 1938).—The Mackay Co., filed with the Commission for a license to add Oslo, Norway as a primary point of communication. By this time, there were as affiliates to Mackay Radio in the International Telephone & Telegraph System, the Postal Telegraph Land Line System, and the Commercial Cable Co. Mackay contended that possession of a direct circuit would allow it and its affiliate companies to more effectively compete with the direct circuit already provided by RCA Communications, as it would become the normal route for all International System traffic between the U.S. and Norway.

The main facts of record are as follows: RCAC controlled the sole direct circuit between the U.S. mainland and Oslo, three cable companies handled traffic between the two countries through transfer to foreign connecting carriers at London and Paris, and Mackay had its Norway traffic retransmitted from a circuit it owned in Denmark. The bulk of traffic between the U.S. and Norway was handled by RCAC's radio facilities, because Norway's Government telegraph administration, which controlled most of the outgoing traffic, received a greater financial advantage from using the radio medium rather than cable. The International System had received about 50 percent of the total revenue accruing to all competing international communication carriers during the previous 2 years.

The transmission arrangements planned for unrouted traffic by Mackay and its affiliate companies would have diverted business from Commercial Cable to the Mackay Radio circuit. The rationale here was that radio wielded a stronger competitive position with respect to U.S.-Norwegian service by way of the Norwegian administration's preference; and this arrangement apparently provided inducement for that government to contract with Mackay. The Commission refuted this reasoning by review of statistics showing that for the previous several years the Norwegian business handled by the cable carriers had held its own or increased as rates comparable with RCAC became effective.

The Commission cited testimony and other evidence in this record as failure to show that the establishment of the proposed route would result in "any improved service to the public":

[T]he same rates will be charged for the same classes of service over the same types of facilities, with no increase in accuracy or speed of service \* \* \*

The evidence does not show any reason to believe that additional traffic will be developed by the proposed circuit. While it is true that the applicant's traffic will increase generally and in particular by reason of making the proposed circuit



the normal route for all International System traffic between Norway and the United States, this will result from a mere shift of traffic from existing carriers to the applicant to the enrichment of the Norway administration and the applicant, to the detriment of other established carriers with no resulting benefit to the public.<sup>23</sup>

A refusal of Mackay's application was supported, the Commission reasoned, by its responsibility to insure that competition would justify a public need, in terms of section 214 and the radio licensing directives of the enabling statute:

\* \* \* In carrying out [the Communications Act], the incidental advantages or disadvantages to particular companies are not controlling. The provisions of Sections 214, 307, 309, and 319<sup>24</sup> of the Communications Act of 1934 indicate clearly that it was not the intention of Congress to permit an indiscriminate extension of telegraph service merely because it might serve the purpose of a particular company to make the extension. The Commission's duty as found in these sections and as interpreted by the courts when construing similar sections of the Radio Act of 1927 and the Interstate Commerce Act is to determine the public interest, convenience, or necessity from the viewpoint of the country as a whole, uncontrolled by the fact that its decision may hinder an applicant in the execution of plans which the Commission has found will bring about a condition contrary to the public interest.<sup>25</sup>

The Mackay Co. appealed for reversal of the decision so as to end what was described as the monopoly of RCAC. It cited sections 311, 313, and 314 of the act to argue mainly that the Congress considered competition in radio be, inevitably, in the public interest. The Radio Commission had, by this reasoning, never refused a license as long as entry would not result in the oversaturation of demand.

The Court held that the Commission did not misconstrue its public interest requirements in this instance by its refusal to grant the license. It reached this conclusion by analyzing the antitrust policy implicit in the Communications Act's radio licensing title, and by referring to court construction of the nonduplication provision in the Transportation Act (evidently in the absence of court analysis of section 214, although this was never referred to here):

Sections 311 and 313 deny licenses to radio concerns which violate antitrust laws. Section 314 forbids acquisition of each other's stock, etc., by radio concerns on the one hand and wire-telegraph or cable concerns on the other, with the purpose

<sup>23</sup> *Mackay Radio*, at 595-96.

<sup>24</sup> While having since been amended and made more definitive, sections 307, 309 and 319 were detailed procedural rules to guide action for radio license authorizations:

Section 307 provided general guidelines for procedure for the distribution of grants, renewals, and revocations of radio licenses, and stipulated length of license terms.

Section 309 contained procedures for notice, hearing, and other action on applications for licenses and filings of protest, as well as conditions to be attached to the operation of facilities under license.

Section 319 contained qualifications and conditions for grants of construction permits as issued prior to licensing.

<sup>25</sup> *Mackay Radio*, at 599-600.



or effect of substantially lessening competition or restraining commerce or unlawfully to create monopoly: To prohibit concerns 'unlawfully to create monopoly' is to recognize that monopoly may be lawful, as most public utility monopolies are. These sections do not show, as appellant's argument implies, that two radiotelegraph circuits are necessarily better than one. Such a belief would be as strange as a belief that two telephone systems, or two railroads, are necessarily better than one. It is obvious that two concerns are sometimes worse than one \* \* \*

The Transportation Act of 1920 requires a railroad to obtain a certificate of 'public convenience and necessity' before constructing a new line, and a finding of 'public interest' before acquiring another line by lease or stock purchase. 49 U.S.C.A. Sections (18-22), 5(2), 20a(2) . . . [T]he meaning of that language throws light on the meaning of 'public interest, convenience or necessity' in the Communications Act of 1934 . . . 'The purpose of the requirement is to prevent interstate carriers from weakening themselves by constructing or operating superfluous lines, and to protect them from being weakened by another carrier's operating in interstate commerce a line not required in the public interest.' *Texas R.R. Co. v. Northside Railway Co.*, 276 U.S. 475, 479, 48 S. Ct. 361, 362, 72 L.Ed. 661. . . .

Appellant's quotations from reports of the former Radio Commission do not show, as appellant contends, that the Commission believed language in the Radio Act of 1927 to require the licensing of competitive radio services wherever the traffic would support them. The quotations show merely the Commission's belief that the statute permitted it to adopt such a policy 'for its own guidance.'<sup>26</sup> Moreover, the statutory language on which appellant relies, which was reproduced in the Communications Act and has been discussed above, will not bear the construction for which appellant contends . . .<sup>27</sup>

The "Oslo" case was the first time that a public utility rationale (i.e., restriction of entry pursuant to section 214) was construed to apply to radio operations. If the public interest standard would advise a "single circuit" in a particular market, then the controlling issue was not to preclude monopoly—the congressional intent of section 314. Rather, the facts of the case argued for control of market entry through section 214, which is exactly what the Court said. This grafting of section 214 issues to radio, as will be discussed, has also occurred recently, in the Commission's rulemaking that allowed open entry the specialized microwave radio transmission industry.<sup>28</sup>

The deliberations of the "Oslo" case considered not only the qualifications of the proposal and the adequacy of existing service, but also tried to determine the contractual intent of the carriers' overseas cor-

<sup>26</sup> See above, p. 23.

<sup>27</sup> 68 App. DC 336, 337-39.

<sup>28</sup> See below, pp. 61-69.

respondent.<sup>29</sup> For national sovereignty reasons, the Commission had no control over the Norway administration other than through the medium of its statutory jurisdiction over the activities of domestic-based carriers.

Implicit in the Commission's reasoning seems to have been a presumption that the "dead hand" of cable posed hardly the danger to radio development as had previously been thought, at least insofar as the United States-Norway route was concerned. The statistical evidence<sup>30</sup> seemed to indicate that the cable carriers held their portion of the market defensively, cutting rates as a holding action against the insensitive relationship of radio costs to distance. The radio carriers had maintained their independence, and, in fact, had managed to secure an impressive share of that market. The market relationship between radio and cable was evidently still viable. The Commission, however, felt that any diversion of traffic from Commercial Cable to Mackay would have been for no other reason than to accommodate the financial interests of the Norwegians and thus to secure a larger share of that route for the I.T. & T. conglomerate. Mackay's forecast for the proposed direct link did not prove to the Commission that the resulting service would be an appreciable improvement over that which already existed.

The "Oslo" case was one of a series of rules, rulings, and regulations which twisted the international industry around from its heritage of competition to the opposite philosophy.<sup>31</sup> Its conclusion was the rationale of the nonduplication intent of section 214, and an explicit standard of "public benefit" for authorizations of competition in the international sector; it denied entry when accomplished either at the expense of carriers already occupying the field or when no service improvements were to be expected.

Thus, from the establishment of the FCC in 1934 to the start of World War II in 1939, applications filed for circuits to countries already served by other American radiotelegraph carriers were generally denied by the Commission.<sup>32</sup> The agency did renew authorizations of competing direct radiotelegraph circuits, recognizing grandfather rights to these existing circuits.

By 1947, the time that the Commission acted on an application filed by Mackay to serve South America from New Orleans, the Commission was cautiously returning to the attitude of encouraging entry:

It is recognized that the policy of the Communications Act is to maintain competition in the international field. It is clear, however, from the act, that this does not mean a blind, indiscriminate policy of authorizing extensions of service by the carriers.<sup>33</sup>

From 1939, the Commission had followed a rather liberal policy of granting applications for new circuits regardless of whether other

<sup>29</sup> See, at 340, the court's support of the Commission's effort on this issue: "[T]he record shows that foreign governments sometimes use the entry of a second radio company into the field as a means of forcing both companies to accept more onerous terms, including a smaller division of the tolls, then were previously imposed upon a single company."

<sup>30</sup> *Mackay Radio*, at 596.

<sup>31</sup> *Ende*, op. cit., III, n. 10, p. 158.

<sup>32</sup> *Mackay Radio and Telegraph Co., Inc.*, 5 Pike and Fischer R.R., 561, 567 (1951).

<sup>33</sup> *Mackay Radio and Telegraph Co., Inc.*, 4 Pike and Fischer R.R., 963, 984 (1947).

carriers were operating to the points concerned. This was due to wartime exigencies; most international traffic at that time was still routed via London. It became necessary in particular to open direct communications facilities to three Commonwealth areas, Australia, New Zealand, and India. Both RCAC and Mackay were authorized to operate direct circuits to these countries.

In January 1942, at the behest of the Defense Communications Board (later succeeded by the Board of War Communications), the Commission adopted as a wartime measure an affirmative policy for the establishment of parallel circuits from the United States to overseas points. If possible, the parallel routes were terminated at different locations. In January, 1943, the Board of War Communications asked the Commission to follow a reverse policy and to allow the establishment of a circuit by a single American carrier to each new point. This policy was retained until May 1945, when the Board relaxed its restriction on the establishment of circuits.<sup>34</sup>

(b) *Radiotelegraph Circuits Between the United States and the British Commonwealth*, docket No. 7094; *Mackay Radio and Telegraph Company, Inc.*, docket No. 7412, 12 FCC 530 (1947).—The reasoning involved in the “Bermuda Circuits” case illustrates that the conventional wisdom at the FCC was returning to the promotion of competition in the international sector. In December 1945, a conference was entered into by the United States and the British Commonwealth to determine what should be done with the direct circuits that the FCC had opened to certain of its countries during the war. The British at that time had regarded them as existing only for the duration of the war and for 6 months after. However, the United States was a premier world power; the British colonies were moving toward independence, and preferred alternatives to London as routing and service points.<sup>35</sup> An agreement was reached that one direct circuit would be installed or retained to each of several countries, a total of 11 circuits. The Commonwealth governments placed in the agreement a clear expression that they would not permit the operation of more than one circuit between the United States and any of these places.

Both RCAC and Mackay expressed an interest in serving all 11 points. The Commission instituted this proceeding to determine which was better qualified to operate; and it discerned a national policy of maintaining competition in international communications, expressly stating that “the applications at issue should be calculated to maintain as much competition between Mackay and RCAC as is feasible under the particular circumstances of this case.”<sup>36</sup> Its dilemma was that, although it granted that RCAC was somewhat more qualified to handle radio circuits than was Mackay, a final decision giving all these points to one carrier would adversely affect, if not destroy, competition. On the other hand, the Bermuda Agreement allowed only one circuit per country, so that the Commission hadn’t the usual alternative of granting both circuits to each point. Therefore, it acted on the suggestion put forward by RCAC to make these grants in reference to the existing structure of the entire field of international communi-

<sup>34</sup> *Mackay Radio*, op. cit., n. 32.

<sup>35</sup> *Ende*, op. cit., III, n. 10, p. 159.

<sup>36</sup> *Radiotelegraph Circuits*, at 533.



cations, rather than the market share of the two carriers. Ultimately, the decision maintained the status quo. The traffic was divided in such a way so as to give to the two carriers a proportion equal to the respective share they had gotten competitively in the worldwide market:

It is apparent in this case \* \* \* that in view of the limitation in the Bermuda Telecommunications Agreement of one circuit to each point, it is not possible to reach a result here of direct competition between RCAC and Mackay as to any of the points at issue. Generally, competition between two carriers regarding any one point of service would be at its sharpest where both operated direct circuits to the point. Since in this case, the Commission has to select one or the other of the two carriers for each point involved, the grantee for each point will have such competitive edge as to service to that point as results from a direct radio circuit. The Commission is, accordingly, confronted with the necessity of applying the policy of competition so far as this can be done within the above limitations \* \* \*.

The Commission is of the opinion, however, that such distribution of circuits should be made so as to give the two carriers the opportunity to obtain about as much traffic proportionately as they now enjoy on a worldwide basis. Each carrier will then begin to operate the direct circuits awarded to it in approximately the same competitive relationship as now exists \* \* \*.<sup>37</sup>

Shortly thereafter, the Commission had to squarely face the issue of competition in the very difficult "Three Circuits" proceeding. It was the first formal hearing since the end of the war in which any carrier applied to operate competitive radiotelegraph circuits. The case was originally referred to as "Four Circuits" when Mackay applied for direct circuits to Portugal, Holland, Surinam (located in northern South America), and Finland. The Finland application was dropped so that the issue became "Three Circuits"; when the Surinam application was denied in formal hearing, it became the "Two Circuits" case. The agency originally made the grant because, though Mackay offered no new rates or service, it felt that there existed a "national policy" in favor of competition. Obviously, this ruling was the exact opposite of that reached in the "Oslo" case, in which the Commission felt bound to prevent the extension of duplicate facilities in instances where the public would receive no particular benefit in terms of rates or service. After reversal on appeal, the issue was reviewed by the Supreme Court. The case was remanded back to the Commission with a holding that there was no policy in favor of competition in an industry so controlled and regulated; and that consequently the FCC had acted without sufficient justification.

(c) *Mackay Radio and Telegraph Company, Inc.*, 5 Pike and Fischer Radio Regulations 561 (1951), rev'd., *RCA Communications Inc. v. FCC*, 201 F. 2d. 694 (D.C. Cir., 1952), aff'd. and remanded, *FCC v. RCA Communications, Inc.*, 346 U.S. 87 (1953); *Mackay Radio and*

<sup>37</sup> Id., at 552-53.

*Telegraph Company, Inc.*, 10 FCC 1321 (1955), *aff'd.*, 238 F. 2d 24 (D.C. Cir., 1956).—The competitive situation to the points at issue was as follows: The Netherlands and Portugal were directly served by RCAC and the cable carriers Western Union and Commercial. Inbound traffic from Surinam was routed almost exclusively via RCAC; outbound traffic was handled competitively by Western Union, All America, and RCAC. In addition, Mackay had secured a minimal share of the three markets through indirect routing. Mackay took the position in the original proceeding that the fundamental issue was whether there should be competition in direct radio telegraph service:

[T]he national policy in international communications favors competition: that a grant of its applications would strengthen telegraph competition in direct radiotelegraph service \* \* \* that while such grant might reduce the traffic and revenues of its competitors, it would not endanger their ability to continue to render a competitive service. \* \* \* [W]ith respect to Portugal and the Netherlands, the present and expected volumes of traffic are sufficient to justify the proposed direct circuits, and are in excess of those between the United States and many other countries to which competing direct radio-telegraph circuits are now authorized by the Commission. With respect to Surinam, Mackay admitted that existing traffic volumes are small, but urged that in view of other considerations, the proposed direct circuit was justified.<sup>38</sup>

Western Union and RCAC contended that Mackay was required to show that the grant would result in some affirmative benefit to the public, and having failed this, its applications should be denied. Their analysis approached the legal questions involved in supplementing an already satisfactory mix of facilities with a circuit providing an identical service, resulting in diversion of traffic from the Mackay affiliate, Commercial Cable:

[T]he law does not require, as contended by Mackay, that competition be extended into new areas, but merely that it should not be artificially stifled by contract. It was also contended that a grant of Mackay's applications would be contrary to the public interest because, without benefiting the public, such grants would result in weakening of carriers now providing the service, and thereby would harm the United States communications system as a whole.<sup>39</sup>

The Commission reviewed these proposed findings extensively, including an examination of the legislative history of section 314 and the conclusion of the antecedent case denying Mackay's application to compete with the single circuit to Norway. Its pertinent considerations were whether a grant of Mackay's application would result in a substantial reduction in competition between cable and radio, and whether it would tend to create an A.C. & R. monopoly<sup>40</sup> in international telegraph communications. It was basically a "single" versus "duplicate" circuit policy question.

<sup>38</sup> *Mackay Radio*, at 570.

<sup>39</sup> *Id.*, at 570-71.

<sup>40</sup> American Cable & Radio Corp., a holding company for I.T. & T. subsidiaries.



The Commission made several findings to justify a grant to the carrier to serve Netherlands and Portugal, a holding opposite of that in the 1936 case. One consideration was the record of growth and change in the industry during those several years: The volume of traffic to Portugal and the Netherlands had more than doubled; therefore the demand, in excess of existing facilities, was more than enough to support Mackay's operations. Its finding on this question was that, despite whatever diversion of the market from Mackay's affiliated cable outfit (Commercial) would result from Mackay's entry, this would not affect the ability of RCAC and Western Union to supply competitive service. Second, there had apparently been a shift in traffic from cable to radio, a trend fed partly, it was acknowledged, by a strong advocacy of radio transmission from government-controlled foreign correspondents. As to this circumstance, the Commission asserted that its own rules and statutory authority would enable it to take action to prevent a carrier from making concessions to an overseas administration detrimental to the interests of the U.S. industry. Third, the Commission reviewed its own licensing practices since the "Oslo" decision to show that it had not followed a "single circuit" policy; a duplicate authorization in this instance would be hardly a break with established practice.

Finally, sections 313 and 314 were cited to the conclusion that "[t]he national policy of the United States is one favoring competition \* \* \* [i]t is clear from a reading of the Communications Act that the national policy in favor of competition as set forth in the antitrust laws has been expressly extended to the field of international communications \* \* \*." The decision referred to "the official cognizance of this policy" in the *Bermuda Circuits* case for support of this reasoning.<sup>41</sup> With two members dissenting, the Commission granted licenses to Mackay to establish communication service to the Netherlands and Portugal. It considered this action as the commencement of a settled policy of encouraging competition in international communications.

On appeal, the order was reversed, with citing from the *Oslo* decision. The Court evidently believed that the Commission had applied its own view of a principle, and a misinterpretation of national policy, authorizing competition for competition's sake. Its holding was that the Commission must decide, in the circumstances of the application, that competition be not merely feasible but beneficial:

In its present decision the Commission points to the large increases in international telegraph traffic and the strong trend from cable to radio since it decided the *Oslo* case in 1936. No doubt such changes make duplication of radio circuits more feasible, but they don't show that competition in this regulated public-utility industry will benefit the public \* \* \*. The Commission's brief on this appeal speaks in general terms of "long range" benefits of competition. But in deciding this case the Commission made no finding that long-range benefits would result from its grant to Mackay, and nothing in its basic findings would have supported such a conclusion \* \* \*. The Commission pointed out that it has

<sup>41</sup> Id., at 581-82.



licensed duplicating radio-telegraph circuits to foreign countries in a number of instances and has renewed such licenses. But it did not say what benefits, or that any benefits, have resulted in any instance.<sup>42</sup>

Finally, in 1953, the arguments were reiterated before the Supreme Court. In order to decide whether the Commission had fairly exercised its discretion to choose among applicants, the Court devised the test of whether the Commission had clearly been guided by "the deposit of experience, the disciplined feel of the expert."<sup>43</sup> The decision, written by Justice Frankfurter, said that no such indication was apparent, entirely apart from the tangible demonstration of benefit for which RCAC contended. To merely rely on competition as a general policy would result in abdication of a primary FCC function—entry control:

That there is a national policy favoring competition cannot be maintained today without careful qualification \* \* \* [That] would most strikingly disregard areas where policy has shifted from one of prohibiting restraints on competition to one of providing relief from the rigors of competition, as has been true of railroads \* \* \* The very fact that Congress has seen fit to enter into the comprehensive regulation of communications embodied in the Federal Communications Act of 1934 contradicts the notion that national policy unqualifiedly favors competition in communications. \* \* \*

Of course, the fact that there is substantial regulation does not preclude the regulatory agency from drawing on competition for complementary or auxiliary support. Satisfactory accommodation of individual industries to the demands of the public interest necessarily requires in each case a blend of private forces and public intervention. The Commission itself has recognized as much by its changing policy toward authorization of duplicate facilities \* \* \* Our difficulty arises from the fact that while the Commission recites that competition may have beneficial effects, it does so in an abstract, sterile way. Its opinion relies in this case not on its independent conclusion, from the impact upon it of the trends and needs of this industry, that competition is desirable but primarily on its reading of national policy, a reading too loose and too much calculated to mislead in the exercise of the discretion entrusted to it. \* \* \*

In reaching a conclusion that duplicating authorizations are in the public interest wherever competition is reasonably feasible, the Commission is not required to make specific findings, of tangible benefit. \* \* \* In the nature of things, the possible benefits of competition do not lend themselves to detailed forecast, but the Commission must at least warrant, as it were, that competition would serve some beneficial purpose such as maintaining good service and improving it. \* \* \* Merely to assume that competition is bound to be of advan-

<sup>42</sup> *RCA v. FCC*, at 694, 698.

<sup>43</sup> *FCC v. RCA*, at 91.

tage, in an industry so regulated and so largely closed as this one, is not enough.<sup>44</sup>

*FCC v. RCA* was a landmark decision in that it affirmed the lower Court's direction that the agency make an affirmative finding of public benefit prior to authorizations of duplication and competition. Presumably, this standard would be a rational application of agency expertise and of the findings of record. As the only issue of industry structure that has ever received hearing before the Supreme Court, this became the watershed case opposing competition *per se* among telecommunications carriers.

Finally, on remand, and after more than 8 years from the date when Mackay first filed its applications,<sup>45</sup> The Commission tried again to reconsider and resolve the grant of duplicate direct circuits.

From the end of the war in 1945, the Commission had granted a number of duplicating circuits and had designated others for hearing. It had also renewed outstanding duplicate circuit authorizations from time to time as the licenses expired. However, the agency recognized that its Court-directed obligation was to arrive at a conclusion for or against duplication on the basis of evidence adduced from the extensive filings. In an almost rote, mechanical manner, the decision recited the findings of record as to improvements made by the two carriers in equipment, facilities, service, and rate reductions. It concluded that, generally, competition between RCAC and Mackay had resulted in these benefits. The Commission granted the authorizations for Mackay to finally enter into business with the Netherlands and with Portugal. The agency felt obliged, however, to avoid mention of any kind of general policy:

We wish to make clear that we are deciding this proceeding on the conclusions we have reached on the basis of the relevant data in the particular case now before us. We are not enunciating a general policy with respect to the licensing of duplicate direct radio telegraph circuits in international telegraph communications, nor do we intend our decision to be construed as an indication that we would, in every future case, authorize duplicating direct international radio telegraph circuits. What we require is that, in order to be successful, an applicant must demonstrate that, as has been done here, through the operation of such a circuit, some public need would be served or some advantage would accrue to the public, or at least that there is a reasonable expectation that such competition may have some beneficial effect.<sup>46</sup>

By this time, the existing mix of radio and cable facilities were in excess of demand, presumably evidence that additional entry would

<sup>44</sup> *Id.*, at 91, 95-97.

<sup>45</sup> The Mackay Co. had applied for direct circuits to the Netherlands, Portugal, and Surinam in 1946, and to Finland in 1947.

<sup>46</sup> *Mackay Radio*, at 1350 (1955). See also *Hawaiian Telephone Company v. FCC*, 498 F. 2d 771 (1974), which was a review of an FCC order granting sec. 214 authority to RCA Global Communications, Inc. to provide private line voice-only service between the U.S. mainland and Hawaii in competition with the Hawaiian Telephone Co. The Court of Appeals for the District of Columbia reversed this action on the ground that the Commission was introducing competition merely for competition's sake, in direct violation of the Supreme Court standard in *FCC v. RCA*.

be infeasible. In spite of this, the Commission felt justified with its "public benefit" finding:

It appears to us that action on our part which would base a denial on the mere existence of excess capacity would enable the present licensee to forestall any possible competition by providing itself with more capacity than necessary. We also note that the existence of extra capacity, especially in the presence of competition, may well be a potent spur to the carrier not only to provide additional service and thereby make more use of the spare capacity, but also gain additional revenue.<sup>47</sup>

To facilitate this point, the Commission noted that the additional service could be provided with a negligible investment and very minor additional annual expenses. Furthermore, the Commission made a finding that "the [international] radiotelegraph industry is not a natural or economic monopoly."<sup>48</sup>

It seems that the Commission came around philosophically to the outlook that induced competition would prompt the carriers to offer premium service and to efficiently plan and utilize their facilities. This rationale was used in 1958 when the agency authorized a new circuit to Mackay after a hearing.<sup>49</sup>

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<sup>47</sup> *Id.*, at 1339.

<sup>48</sup> *Id.*, at 1236.

<sup>49</sup> *Mackay Radio and Telegraph Co., Inc., et al.*, 25 FCC 1197, 1239 (1958).



## ▼. THE IMPLEMENTATION OF POLICY

### *A. Domestic common carrier*

A.T. & T. has historically undertaken the construction of new plant for the benefit of both existing and future ratepayers, i.e., to maintain and expand existing levels of service and to introduce new communications offerings. Today's interstate toll network is the product of an effort to increase overall service quality through the maintenance of substantial capacity.

Nevertheless, it appears that the efficiency of providing and utilizing this network has a substantial impact on A.T. & T.'s allowed rate base, and thus has implications for the FCC's section 214 enforcement program over the acquisition and operation of major facilities. The Commission may not be capable, however, of undertaking thorough, systemwide audits of A.T. & T.'s plant. These were the implications of a 5-year assessment of the Bell System's interstate construction and acquisition program and associated rate base and revenue requirements.

The telephone company has also provided discrete local CATV distribution to entrepreneurs who would otherwise be obliged to undertake construction on their own. The FCC has imposed section 214 jurisdiction on this service as an element from which the major communications carriers receive their aggregate return. What follows is a discussion of the Commission's findings and conclusions in docket 19129 with regard to network management and construction, and of its review in *General Telephone Co. of California* of the provision of local cable television facilities. In order to comprehend the size, complexity, and dispersion of the interstate network, and the function and predominance of switches, a brief description is provided of the present-day system. This is also the point of departure of the Commission's judgment in the docket 19129 proceeding.

#### *1. Rate base control*

##### *a. Network management*

(1) *The modern network.*—The toll switching model of 1930 was revised in the early 1950's to allow a natural outgrowth to the present-day system of nationwide customer dialing. Today's general toll switching plan consists of a five-level hierarchy of switching offices, with a maximum of nine switched connections used on any call. The basic capabilities of the newer system include three- and six-digit translation for routing, and automatic message accounting to record billing information. But the primary function of the present plan is automatic alternate routing—the use of an electromechanical switch to redirect calls to an alternate trunk group when all the trunks in a direct group are busy. One “final” trunk group, by handling the overflow from many high-usage routes, may be operated at both high oc-

cupancy and sufficiently low blockage to guarantee low overall blocking to customers. Furthermore, a judicious division of the traffic load between direct and alternate routes yields a telephone network costing less than a nonalternate route network carrying the same amount of traffic.<sup>1</sup> The prewar system of crossbar switches was adapted to these expanded requirements, and entailed new operating company methods and traffic rules to interconnect switching offices.

Prior to the conversion to direct-distance dialing and electromechanical switches, the queueing and switching functions performed by long-distance operators was designed to establish high blocking rates in order to keep the costly toll circuits occupied a greater percentage of time.<sup>2</sup> The greater the occupancy, the longer the queueing delay. Engineering delay of 30 seconds was typical in 1950, before the introduction of direct distance dialing.

Because "delay" operation was impractical without an operator, a change to direct distance dialing required low blocking on toll networks. Sufficient capacity had to be provided to insure a lower probability that a call would be blocked and result in an "all circuits busy" signal to the caller. Since low blocking implied lower circuit utilization of a greater number of lines, direct distance dialing had to be introduced without increasing investment in transmission plant. Alternate routing by electromechanical switch was the answer.

This entailed a network that would fully utilize toll switching, not to limit it as was the original intent of the general toll switching plan of 1930. The high usage and final trunk groups were not to be engineered only for long-distance traffic as they were in the pre-war decades. Nor were these lines to be limited to the carriage of separable interstate or intrastate toll traffic. Today's network handles all toll traffic regardless of its identity. For example, it is quite possible, and indeed common, for a toll call intended between cities within a single State to be automatically routed to its destination through out-of-State lines at a higher level in the switching hierarchy. Engineering of toll trunks and switches, therefore, is accomplished on a comprehensive basis to insure automatic alternate routing achieves the maximum utilization of all telephone plant.

Automatic alternate routing requires some measurement of usage and capacity to assess overall performance. A.T. & T. measures circuit usage as the proportion of time the average trunk in a group is used during the busy (peak) hour of the busy season, and the aggregate of trunk groups is engineered for high peak occupancy. Because calls arrive on a given trunk essentially at random, in accordance with the operation of low blockage, 100-percent utilization is never achieved in practice. The incidence of blockage is measured as a function of the number of trunks and trunk groups, more explicitly, the number of calls blocked in a particular group because no trunks are available. A.T. & T. has sought to achieve the goal of accommodating 99 percent of the calls offered to a final group in the busy hour of the average business day of the busy season. Since blockage is measured under the most extreme conditions, very little actual blockage occurs, and the actual quality of service for most periods of time is usually higher than this figure.<sup>3</sup>

<sup>1</sup> Macurdy and Ritchie, *op. cit.* III, n. 1.

<sup>2</sup> See discussion above, pp. 17-18.

<sup>3</sup> Docket 19129, below, p. 36. Final Decision at 50-51.

These procedures and standards are centrally coordinated through A.T. & T.'s network management program, balancing circuits and switching equipment on a continentwide basis in order to insure the maximum utilization of facilities and the completion of as many messages as possible (this is a continentwide activity because the American telephone network is integrated with that of Canada). Network management was established in 1963 after A.T. & T.'s discovery from experience that the switched network had to be comprehensively monitored and controlled to insure trouble-free, efficient utilization.

(2) *The "Switch-in-Network."*—As the network has been modernized over the past generation, the importance of switches, which once (as manual toll boards) represented a small portion of plant investment, have so increased that they currently represent one of the largest portions of a carrier's investment in operating plant. This has been true particularly as No. 1 electronic switching systems (EES) have been installed to supplement the capacity of the electromechanical No. 4A toll crossbar. Based in part on computer technology, the newer electronic systems appear to have the technical potential of providing new information services such as credit authorization and electronic funds transfer. Some feel that because of their financial importance and capacity for sweeping social and industrial changes, switches can no longer be ignored as questions of regulatory control.<sup>4</sup> This viewpoint is held particularly in the context of whether forecasts might prove incorrect of these services' great revenue potential. In this event, regulation is advocated in order to make revenues sufficient to return the carriers' investment, and so prevent cross-subsidies from monopoly services.

(3) *Charges for Interstate Telephone Service (docket 19129), phase I, 38 FCC 2d 214 (1972), phase II, Initial Decision, 64 FCC 2d 131, Final Decision, 64 FCC 2d 1 (1977).*—This investigation was the FCC's response to interstate rate increases filed by A.T. & T. in 1970. The agency concluded in phase I that Bell should be permitted to earn a minimum return of 8.5 percent on its interstate plant. A.T. & T. was allowed to file rate adjustments for its MTS and WATS services that were designed to accrue revenues to achieve that goal. Concurrently with the ongoing phase I proceeding, phase II of docket 19129 was designated as a broader inquiry into all the expenses that compose the telephone company's rate base, to which is applied the percentage rate of return in determining its allowable earnings. (Phase II also assessed the effects of vertical integration on A.T. & T.'s procurement practices.)

The Commission said that the traditional method of valuating the "used and useful" portion of carrier plant is based on two counteracting principles, the fifth amendment rights of the utility, and the necessity for control of rate levels through judicious rate base valuation. This tension is implicit in the rate base control purpose of section 214, since that section actually relates the "used and useful" standard to rate base regulation:

\* \* \* The idea of basing utility rates on the value of the assets used and useful is rooted in American legal theory and particularly in the constitutional limitations on the taking

<sup>4</sup> See, e.g., S. 611, Communications Act Amendments of 1979, U.S. Senate, Committee on Interstate Commerce, 96th Cong., 1st sess., introduced by Senator Hollings (Mar. 12, 1979), which amends sec. 214 to assert jurisdiction over switches.



of private property for public use. \* \* \* Accordingly, courts have felt that the owners of public utilities must be compensated for the use of their property in providing service to the public. In view of its origins, it was only to be expected that judicial and regulatory inquiry should focus on the idea of compensating the utilities' owners for the use of their property in providing public service.

Equally central to the used and useful concept, however, is the equitable principle that the ratepayers may not fairly be forced to pay a return except on investment which can be shown directly to benefit them. Thus, imprudent or excess investment, for example, is the responsibility and coincident burden of the investor, not the ratepayer.<sup>5</sup>

Phase II drew the overall conclusion that the Commission's section 214 authorization procedures needed regular reporting to permit better oversight of the telephone company's programs of construction and network management, both of which were regarded as directly affecting the value of A.T. & T.'s rate base. This implied that greater regulatory attention must be paid to the engineering of the telephone network in advance of acquisition and operation of major facilities.

The *Initial Decision* in phase II had concluded that neither the State commissions nor the FCC had ever conducted in-depth review of A.T. & T.'s construction plans department and operating company construction budgets. The final decision concurred, after reviewing the telephone company's service requirements and engineering standards. It discovered that the aggregate of its trunk groups were engineered for greater peak usage and lower blockage than had actually been needed for the test years 1969-72. Although caused by errors in planning, this inferred excessively high overall quality of service. In economic terms, this result is a measurable phenomenon of diminishing returns: Service improvements decrease at progressively greater levels of investment. The indication was of an excessive amount of underutilization and idle plant, hence "much excess capacity and thus a general over-building of the interstate toll network."<sup>6</sup> The Commission acknowledged, however, that it must bear some responsibility for this situation because of its obligations under section 214:

\* \* \* A.T. & T. accepts some responsibility—as it reasonably must—for the chronic forecasting errors which have led to present network underutilization. However, we also agree that, because of our authorization authority under section 214 of the Communications Act, this Commission must also bear some responsibility for the present situation. \* \* \* We agree with A.T. & T. that continuing network management and planning of future construction to avoid inefficient usage is vital. Consequently, we shall direct the staff of the common carrier bureau to develop regular reporting requirements and changes to our section 214 authorization procedures which will permit better oversight of network management and utilization. In the interim, we shall require A.T. & T. to demonstrate as part of its regular section 214 justification, that any

<sup>5</sup> *Phase II, Final Decision*, at 47 (references omitted).

<sup>6</sup> *Id.*, at 51.

proposed addition to the network will not exacerbate the present underutilization of the network and to take remedial action to correct that which presently exists \* \* \* [T]his Commission [also] needs more effectively to review the Bell System's construction program \* \* \* [W]e shall require A.T. & T. to submit to the staff periodic reports on various aspects of its construction program which have a bearing on the matters we discussed above with respect to the underutilization of the interstate network. We shall further direct the common carrier bureau staff to develop more effective oversight procedures as discussed [above].<sup>7</sup>

Docket 19129 did not focus on switching facilities as a matter of section 214 oversight, although the *Initial Decision* discussed A.T. & T.'s switching installations in high-usage metropolitan areas.<sup>8</sup> It also criticized the trial staff's challenge of A.T. & T.'s switching procurement methods as an exercise in hindsight unfair to carrier management.<sup>9</sup>

#### b. Local distribution facilities

The FCC has made clear that the telephone company is subject to section 214 regulation when it constructs an interstate "channel of communication" pursuant to furnishing any common carrier service. The reasoning in *General Telephone Co. of California et al.*<sup>10</sup> determined the reach of section 214 to the construction of wire distribution facilities for CATV systems, a common method of providing local channel capacity to subscriber premises. These networks are discrete and are not interconnected with any telephone exchange or toll service facility. The conclusion was devised according to the 1933 *Southwestern Bell* decision in order to enable the Commission to control additions to the carrier rate base. *General Telephone* consolidated the certification issue from several dockets which were reviewing the lawfulness of tariffs establishing pole line attachment arrangements and other services provided by carriers to CATV operators.

The Commission had held that the furnishing by telephone companies of channels of communication to CATV operators "is clearly a common carrier undertaking."<sup>11</sup> The decision in *General Telephone* came shortly after the Supreme Court ruling in *United States et al. v. Southwestern Cable Co. et al.*<sup>12</sup> which upheld the Commission's authority to regulate CATV systems; that decision had classified CATV channel service as interstate communications even if originated from the same State in which the particular system operated.

The General Telephone System and the Bell System companies approached the issue as the furnishing of a purely local service, and hence exempt from the FCC's jurisdiction: The television broadcast loses its identity at the CATV system headend, where it is processed

<sup>7</sup> *Id.*, at 51-53 (reference omitted).

<sup>8</sup> *Id.*, at 336-41.

<sup>9</sup> *Id.*, at 319; see also the general remarks of the *Initial Decision* at 489-90.

<sup>10</sup> 13 FCC 2d 448 (1968).

<sup>11</sup> *Id.*, at 454; see *Common Carrier Tariffs for CATV Systems*, 4 FCC 2d 257 (1966).

<sup>12</sup> 392 U.S. 157 (1968).

and retransmitted over the cable; consequently, there existed no through interstate communication. The carriers also argued that since the input and output points of each system are located within the confines of one State, the transmission was purely intrastate. Furthermore, the local facility was contended to be a local branch line within the meaning of the exemption in section 214(a)(2), as well as local exchange service within the meaning of section 221(a) of the Communications Act.

The Commission developed the premises for its action in the following manner: [t]he telephone company participates as a link in the continuous, unaltered relay of television signals to the viewer (since CATV systems fill much of their channels with the importation of distant television signals), and is thus performing an interstate communications service irrespective of the location of the carrier facilities. In conjunction with *Southwestern Cable* and the FCC's ruling in *Common Carrier Tariffs*, this basically established the rationale for Federal intervention. Second, while most of the construction at issue did not cross any State boundary, the Commission cited *Southwestern Bell* to reject the premise that only intrastate channels of communication were involved:

Neither the wording of this definition [of the term "line" in the Communications Act] nor anything in the legislative history of section 214 indicates a congressional intent to limit the certification requirements thereof to cases where the physical facilities of the common carrier cross a State boundary. On the contrary, we believe that the definition of a line manifests a primary congressional concern over the channel of communication, rather than merely over the wires and cables; that is, the equipment used to establish the channel. Our view is reinforced by the fact that section 214 is not confined to the "extension" of a line—which might reasonably be construed as requiring some part of the common carrier facilities to cross a State boundary—but includes the "construction of a new line" even though wholly within a single State so long as it is part of an interstate "channel of communication" or "line." *Southwestern Bell Telephone Co.*, 6 FCC 529, 532 (1938). The broadcaster's signal is an interstate channel of communication and the CATV channel distribution system which is a link in the transmission of the signal to the television set of the viewer is a part of that interstate channel. Significantly, the telephone companies have been unable to point to anything in the statutory scheme of the Communications Act which would justify limiting the phrase "channel of communication" to a common carrier channel.<sup>13</sup>

The Commission quickly disposed of the contentions that the service constituted the exemption from Federal regulation as "local, branch, or terminal lines not exceeding 10 miles in length" and as local exchange service:

Essentially, the exemption is intended to apply to minor additions or improvements to existing facilities or services and the expenditure involved is ordinarily small.

<sup>13</sup> *General Telephone Co.*, at 457-58 (reference omitted).



The construction under consideration in this proceeding, however, involves far more than a minor addition for the improvement or "filling in" of existing services. The channel facilities necessitated a considerable amount of new construction by the telephone companies in order to provide new customers with a type of service significantly different from that theretofore provided in the said communities.<sup>14</sup>

\* \* \* \* \*

The construction attributed by the carriers to the phrase "telephone exchange service" must be rejected as inconsistent with the plain meaning of the words used. Manifestly, the phrase is intended primarily to apply to a telephone or comparable service involving "intercommunication;" that is, a two-way communication, not the one-way transmission of signals which takes place with respect to CATV channel service. Furthermore, such channel service does not require an exchange, does not go through an exchange, and is totally unrelated to the "exchange service charge." \* \* \* Since section 221 (b) is not even remotely applicable to the construction of lines for CATV channel distribution service, we need not concern ourselves with the extent of any local government regulation of telephone exchange service.<sup>15</sup>

The decision reviewed Supreme Court construction of section I (18)–(22) of the Interstate Commerce Act to the effect that "the building of unnecessary lines involves a waste of resources and that the burden of this waste may fall upon the public[.]"<sup>16</sup> In conjunction with its reliance on *Southwestern Bell*, this reference clearly indicated that the Commission was pursuing its legislative directive to control additions to the rate base. Cease and desist orders were issued on pending construction in several systems until section 214 certificates were applied for and issued.

## 2. Industry structure

### a. "Open Entry"

Throughout most of this century, domestic local exchange service and long-distance transmission have retained the market and regulatory structure that gained credence during the early decades. Communications suppliers, technologies, and the services they rendered were largely homogeneous and easy to classify. Startup operations, and the planning, extension, and maintenance of service demanded substantial capital and annual expense. The Commission required an application for the construction, extension, acquisition, or operation of any new channel of communication or transmission thereby, and the same was imposed on the discontinuance, reduction, or impairment of service. Competition between Western Union and A.T. & T. for private line services remained until recently the sole exception to the boundaries of monopoly that remained around the entire industry.

<sup>14</sup> *Id.*, at 459.

<sup>15</sup> *Id.*, at 460.

<sup>16</sup> *Id.*, at 456, citing *Texas & Pacific Railway Co. v. Gulf, Colorado & Santa Fe Railway Co.*

Today, neither the Bell operating companies nor the independents are franchised by regulatory agencies to operate in areas served by one another; and Western Union has held a monopoly in public message telegraph service since 1943. Nonetheless, the generalization no longer holds that only one communications entity can serve a single geographic area most efficiently.

While telephone exchange service has been retained as a local monopoly, local operating companies provide intracity distribution facilities to a new class of communications suppliers called specialized common carriers. These microwave radio systems have captured a small share of the data communications market; as have domestic satellite systems and "value-added" carriers—companies which lease transmission lines from the "underlying" supplier and add extra capacity to offer such services as packet-switched data and facsimile networks. There are also shared users, which provide communications service on a nonprofit basis, and a greatly expanded number of private communications systems, which were once limited to railroad and other right-of-way companies.

This new industry structure had its beginning in 1959. At that time the FCC began to favor new entry with respect to the use of private microwave systems<sup>17</sup> and later the grant to Microwave Communications, Inc. (MCI) to construct a network between Chicago and St. Louis.<sup>18</sup> The Commission proceeded in a market-by-market fashion to implement an "open entry" policy which has enlarged the number of submarkets and competitive vendors available to specialized users.

Authorizations of point-to-point terrestrial microwave stations, with associated towers and dish-shaped antennae, require title III licensing as does radiotelegraph. The Commission's new policy was nonetheless fashioned as a section 214 entry question, and its rationale was explained in accordance with the *RCA* opinion. The FCC has had difficulty, however, in maintaining control over the scope of authorized entry, as MCI's Execunet service illustrates. What follows is a brief explanation of the characteristics of the data transmission market and the policy issues it raised, and a review of the formulation of the Commission's stance in the *Specialized Common Carrier Services* decision. The philosophy of that decision was extended to open entry of resale arrangements, and a determination of was made of section 214 jurisdiction over these entities which compete through service extensions rather than facility ownership. Also discussed are the court directives for section 214 treatment of services which duplicate message telephone service.

Microwave transmission, which was developed during World War II, requires relatively little capital investment for the startup and maintenance of a system. Within 15 years, its capacity for data communication and general flexibility seemed suitable to meet the emerging demand for computer networks. This innovative medium had also been coming into use in conjunction with the coaxial cable facilities of the voice-switched network. It was a matter of question whether this technology demonstrated the existence of economies of scale for the purpose of serving the customized market, requiring a certain level of

<sup>17</sup> *Allocation of Frequencies in the Bands Above 890 Mc.*, 29 FCC 359 (1959).

<sup>18</sup> *Microwave Communications, Inc.*, 18 FCC 2d 953 (1969), reconsideration denied, 21 FCC 2d 190 (1970).

demand to attract entry and introduce service. Since the new market was of recent origin, with no clear relationship to the services offered by the established carriers, the Commission could not expect guidance in the Communications Act for regulating it.

After MCI was permitted to establish its initial route, several other groups, some affiliated with that carrier, began seeking to enter the market, proposing nation- or region-wide networks. A general endorsement of market entry constituted an issue of economic impact on A.T. & T.'s existing services; and a new policy was considered in the context of duplication and public need.

(1) *Specialized Common Carrier Services (docket 18920)*. *Notice of Inquiry*, 24 FCC 2d 318 (1970), *First Report and Order*, 29 FCC 2d 870 (1971).—Docket 18920 was instituted to facilitate the handling of title III radio license applications by determining “[w]hether as a general policy the public interest would be served by permitting the entry of new carriers in the specialized communications field[.]”<sup>19</sup> The *First Report and Order* created a Commission policy in favor of new entry with the observation that there existed a large potential market and a public need and demand for the proposed services. It anticipated that this philosophy would result in no degradation to the regular telephone service provided by the established carriers.

In adopting this policy, the Commission noted that the specialized communications market, particularly for data transmission, was growing and would continue to expand very rapidly. The new carriers were “seeking primarily to develop new services and markets, as well as to tap latent, but undeveloped submarkets for existing services . . .”<sup>20</sup> The record indicated, the Commission felt, that “entry by more than one private-line carrier should be generally reasonably feasible, in view of the large potential market and it (sic) heterogeneous character.”<sup>21</sup> It noted also that the proposed plant investment and revenue requirements were not of a magnitude anywhere near those of an A.T. & T. or even a Western Union. In a market of this type and size, the Commission said, a number of small but viable carriers may be able to coexist in any particular region. It regarded as unlikely the prospect that facilities duplication would bankrupt all competitors, leaving no one to provide the service; the demise of a carrier would simply result in the customers’ shifting to another commercial entity.<sup>22</sup>

The established carriers and related interests argued that this analysis did not comport with the applicable legal standard for authorizing new entry. Specifically, they referred to the standards of section 214 and of the Supreme Court decision in the *RCA* case. It was asserted that under section 309, in which the applicant for a radio license is a carrier, the Commission must apply the standards of section 214. The carriers pointed out that the statute was enacted to avoid wasteful competition and uneconomic duplication of facilities. Consequently, the argument continued, section 214 “requires a finding that there is a need for the proposed services which existing carriers are not now adequately meeting and could not in the future adequately meet.”<sup>23</sup>

<sup>19</sup> *Notice of Inquiry*, at 327.

<sup>20</sup> *First Report and Order*, at 906.

<sup>21</sup> *Id.*, at 925.

<sup>22</sup> *Id.*, at 925–26.

<sup>23</sup> *Id.*, at 900. The proposed standard was reintroduced in H.R. 12323, the *Consumer Communications Reform Act of 1976*. See generally, U.S. House of Representatives, Committee on Interstate and Foreign Commerce, *Hearings on Competition in the Telecommunications Industry*, 94th Cong., 2d sess. (1976).



Presumably, this standard would influence any benefit of the doubt, based on the evidence and the agency's experience, in favor of the established carriers to react to market demand and introduce service.

The Commission concluded that this test was too narrow a construction of its responsibilities under sections 309 and 214. The adequacy or capacity of the established carriers to meet future requirements should not be the determinative factor of new entry, "where growing future traffic is involved and new services are proposed."<sup>24</sup> It questioned whether the major carriers, whose facilities and practices were developed on the basis of serving a large and steadily growing market for voice communications, could or should be expected to respond to computer users' needs. Based on its "cumulative knowledge" of the industry and evidence in the record, the Commission perceived "sufficient ground for a reasonable expectation that new entry here will have beneficial effects."<sup>25</sup> Small, specialized entities would provide flexibility and a wider range of choice to a data communications market that was much smaller than that serviced by the switched voice network, was growing more rapidly, and had different operating characteristics. The Commission believed that this judgment adequately treated the standards of the *RCA* case.

Furthermore, there existed "no uniform requirement [in public utility law] that new entry may be authorized only if existing carriers are unable or unwilling to provide the proposed services."<sup>26</sup> The consensus of case law and public utility literature seemed to be that the public should not be deprived of the benefit of new and improved services solely because of the prospect of traffic diversion; and the adequacy of the existing market was only one element of importance to be considered when assessing the desirability of competition.

Since this rulemaking, the Commission's policy toward small, specialized carriers has been to permit them to grow and coexist with a message toll monopoly characterized by economies of scale and large capital requirements. All carriers operating through the microwave radio spectrum enter into service through the issuance of title III radio licenses subject to 5-year renewals. The Commission grants permission for the operation or extension of new lines through section 214 rather than title III construction permits. The section 214 procedure is used because, unlike radio broadcast operations, radio carriers derive point-to-point "channels of communication" from the spectrum. In addition to the fact that both the specialized and established carriers must file tariffs under title II, it is apparent that the "open entry" policy is qualified in accordance with economic impact considerations.

(2) *Packet Communications, Inc.*, 13 FCC 2d 922 (1973).—Packet Communications Inc. proposed a "packet switching" service by which small groups (packets) of digitized data are transmitted to computers through a "store and forward" operation. The service was to be offered over channels leased from other carriers. The *PCI* decision was the first time that the Commission ruled on the capabilities of "value added" carriers. *PCI* submitted a section 214 application to initiate its service, and it stated that it was willing to have itself treated as a traditional common carrier until the Commission should decide its policy toward such service. The *Resale and Shared Use* proceeding

<sup>24</sup> *Id.*, at 909.

<sup>25</sup> *Id.*, at 910 (reference omitted).

<sup>26</sup> *Id.*, at 902 (reference omitted).

ultimately determined the question of jurisdiction over entities that offer specialized communications service through facilities that they do not own.

There was some question expressed in comment on the *PCI* application whether such carriers should be subject to the section 214 certification requirement, and whether the economic impact issue involved in the new offering had been adequately treated. The FCC referred to its *Specialized Common Carrier* decision to rule that Packet Communications, Inc. would serve a growing market that was not being satisfied at the time by existing carriers:

[W]e recognize that the entry of "value added" carriers such as PCI into the market for communication services will of course impact upon the structure of industry. It will, however, introduce new and improved means by which users having data transmission requirements may satisfy those requirements in a manner not now available from any generalized or specialized carrier. \* \* \*

Further, it is our opinion that the services PCI initially will offer the public over its proposed facilities would constitute PCI a common carrier within the meaning of section 3(h) of the Communications Act and thus subjects PCI to the certification and other requirements of title II of the Communications Act. \* \* \*

It is apparent that there is a growing market to be serviced by such operations and that existing common carrier services are not now available to satisfy the demands of that market. In this respect, we feel that the findings and philosophy reflected in our *Specialized Common Carrier* decision in docket 18920 dealing generally with the market for data transmission and other specialized services are relevant and opposite here and support a competitive environment for the development and sales of the type of services proposed by PCI.<sup>27</sup>

(3) *Resale and Shared Use of Common Carrier Services and Facilities* (docket 20097) 69 FCC 2d 261 (1976).—The Commission noted in *Resale and Shared Use* that its *Mackay Radio* decision of 1938<sup>28</sup> had mandated title II jurisdiction generally, and certification under section 214, for the lease of a telegraph circuit into an area not previously served, even though the carrier's use of the leased line was not exclusive.<sup>29</sup> The threshold question in this broad rulemaking, however, was whether entities which do not own their own transmission

<sup>27</sup> *Packet Communications*, at 924–25. See also, *Graphnet Systems, Inc.*, 44 FCC 2d 800 (1974); *Telenet Communications Corp.*, 46 FCC 2d 680 (1974). Also, in the *Overseas Data-phone Decision*, docket 19558, 57 FCC 2d 705 (1976), the Commission documented a substantial potential for growth in the international data communications market. It also found that the services provided by the international record carriers needed to be supplemented with more cost effective specialized capability. Consequently, it granted applications filed pursuant to sec. 214(a) by Graphnet, Telenet, RCA Globecom, and Western Union International, Inc., to provide overseas data communications through their domestic networks. See *Graphnet Systems, Inc.*, et al., 63 FCC 2d 402 (1977). The decision made it clear that the Commission was not at that time formulating a general entry policy, but rather wished to supervise and evaluate the new service offerings in order to "more fully ascertain the exact contours of the public benefit in the provision of these services, and where appropriate, delineate future policy concerning these overseas data communications services." at 407.

<sup>28</sup> See above, p. 63.

<sup>29</sup> *Resale and Shared Use*, at 307.

facilities must resell (with or without "adding value") or share communications services as regulated activities under title II.

The Commission felt that, as far as the public was concerned, the status of resale offerings was the same as those acquired from traditional common carriers—they are supplied indifferently to all users on a first-come, first-serve basis. Accordingly, resale carriers were to be subject to section 214 for both entry and exit purposes. There was to be no showing required that the proposal "adds value" to the underlying facilities, nor was there to be a demonstration of need for the service, or of the economic impact of entry. In general, and consistent with the *Specialized Common Carrier Services* decision, "open entry" was made the rule for resale:

We here warrant, as we did in the *Specialized Common Carrier* decision, that entry of resellers and the expansion of shared use will have beneficial effects and will outweigh any possible detriments. Insofar as the entry of new resellers will duplicate services of existing resellers, we find this fact not to be a barrier where the public interest will be served.<sup>30</sup>

Because they do not offer services for a profit, sharing arrangements were not to be subject to common carrier regulation, and the Commission adopted no other regulations or reporting requirements over shared services.

In the evaluation of a resale applicant, only the usual fitness criteria would be applied, i.e., that it is technically, legally, and financially qualified to enter the market. The Commission also said, however, that the section 214 application must specify the number and nature of the "channels of communication" required. If, in instances of network reconfiguration, the carriers' requirements exceed the number of channels authorized, an additional application was to be submitted and acted upon. Nor were resellers to constitute an exception to the requisite authorization of multiplexing equipment, "because this is a creation of new 'lines' or 'channels' under section 214."<sup>31</sup> This was also to include network expansion through the operation of switching centers. Nonetheless, the Commission saw no reason to change its position on switching equipment. Certification of switching "as part of a complete transmission service" was not required.<sup>32</sup>

### b. The Scope of Open Entry

While the *Specialized Common Carrier* decision concluded that duplication and entry in the private line market was possible and would serve both present and future needs, it did not define what a private line service was.<sup>33</sup> Although service definition is essentially a marketing question, in utility regulation it may have an industry

<sup>30</sup> Id., at 311 (reference omitted).

<sup>31</sup> Id., at 312.

<sup>32</sup> Loc. cit.

<sup>33</sup> See, e.g., *Specialized Common Carrier*, at 875: "According to MCI, the 'real distinction which delineates MCI service from anything provided today by existing common carriers is not the facility itself but the manner in which a customer may utilize it in order to provide a customized intra-company point-to-point communications system of his own design and capability.' . . . There is, MCI says, 'a distinct difference between a public telephone service which is a natural monopoly and a customized communications service offered on a private point-to-point basis.'" The decision cited MCI's rather generalized pleading without further qualification.



structure goal of insuring that any barriers to entry are equitable and do not preclude the introduction of essential service. Consequently, the specialized carriers favored a broad definition of private line service while the established actors in the industry argued that the FCC must confine the competitive segment of the transmission market. A.T. & T. argued that private line services did not constitute a "market" at all. It regarded some classes of specialized service as amounting to an alternative, for many users, to ordinary long-distance telephone service or WATS. The ultimate result of duplication, it was contended, would occur through the mechanism of "cream skimming": new entrants would concentrate their business on high-profit routes. This would cause revenue diversion, would debilitate the rate structure that supports both local exchange service and high-cost long-distance routes, and would generally force the alternate rate method of cost-based pricing.

A test of defining the limits of competitive entry was demonstrated recently in litigation over MCI's Execunet service. Introduced in 1974, the FCC regarded Execunet as a prototype alternative to public message telephone service, and endeavored to terminate it. The Commission had, however, recently waived the proposal in docket 19117 for any prior approval requirement for new services instituted over authorized facilities. In 1976, oral argument was heard on the legality of the Execunet tariff, and it was disallowed as not an authorized service under the *Specialized Common Carrier* decision. This was reversed on appeal, with the D.C. Circuit Court ruling that the FCC had misread its own language in *Specialized Carriers* and had too broadly interpreted its discretion under section 214 to reach duplication through control of new services. What follows is a review of the FCC's action in docket 19117 and of the court's rejection of that agency's reasoning of the Execunet issue.

(1) *Establishment of Rules Pertaining to the Authorization of New or Revised Classifications of Communications on . . . Common Carrier Facilities (docket 19117)* 39 FCC 2d 131 (1973).—In 1971, the Commission issued a *Notice of Proposed Rulemaking*<sup>34</sup> in docket 19117 which looked toward the adoption of rules governing the adoption or discontinuance of service. The docket was to consider whether domestic carriers should be required to get Commission approval before filing tariffs for services not previously set out in a section 214 application. The purpose of the proposal was threefold: to decide the public interest ramifications of a service before it was commenced, thereby protecting the public from service disruptions that might be caused if the service was allowed to go into effect and later enjoined; to put general domestic carriers (such as AT&T and Western Union), which would previously start a new service simply by filing a tariff, on an equal footing with international and domestic miscellaneous carriers whose facilities authorizations were always restricted so that new services required further section 214(a) proceedings; and to protect specialized carriers, who also needed prior approval of entry under section 214(a), from unfair competition from the generalized carriers.<sup>35</sup>

<sup>34</sup> 27 FCC 2d 36 (1971).

<sup>35</sup> *Id.*, at 28–39.

The proceeding was terminated in 1973<sup>36</sup> with the reasoning that any requirement for prior approval of new or revised service offerings would "delay the establishment of service and, in fact, inhibit realization of our policy objectives in docket 18920." The Commission decided, in essence, that, in the absence of restrictions imposed under section 214 facilities authorizations, new services offered over existing facilities would be regulated, if at all, under the tariff provisions of the Communications Act rather than as section 214 certification requests. The Commission recognized that this made "it possible for domestic carriers, as a general rule, to offer new classes or subclasses of communications service over duly authorized facilities merely by filing appropriate tariff revisions" pursuant to the FCC rules and sections 203, 204, and 205 of the act.<sup>37</sup>

(2) *MCI Telecommunications Corp.*, 57 FCC 2d 271 (1975), 60 FCC 2d 25 (1976), reversed, *MCI Telecommunications Corp. v. FCC*, 182 App. D.C. 367 (D.C. Cir., 1977), cert. denied, 434 U.S. 1040 (1978).—In 1974, MCI issued tariffs for a class of "metered use" services, among which was Execunet,<sup>38</sup> to be marketed as a private line offering. This action provoked a great deal of uncertainty concerning the applicability of dockets 18920—*Specialized Carriers*—and 19117 to the marketing of services that are substitutable for those, such as MTS and WATS, which were presumed exclusively limited to the telephone company.

In 1975, A.T. & T. complained to the Commission that Execunet was a functional equivalent of long-distance message telephone service and that no such offering could be tarified by MCI. The FCC informed MCI that, as distinct from the monopoly switched telephone services furnished by A.T. & T., its section 214 authorizations limited the use to its section 214 facility authorizations and Commission policies. The Commission decided that "the combination of \* \* \* similarities" between Execunet and MTS made Execunet "essentially a switched public message telephone service \* \* \*," and terminated the Execunet tariff by letter order.<sup>39</sup> This order was stayed by the District of Columbia Circuit Court, citing ex parte contact violations on the part of the Commission.

The FCC then accepted comments and heard oral argument on the matter, and issued an opinion based on a review of the *Specialized Common Carrier* decision. The threshold question was whether MCI was permitted to offer Execunet or any other of its services pursuant to its section 214 facility authorizations and Commission policies. The Commission announced that it would not consider any benefit to the public resulting from Execunet in determining its legal status.

The Commission took the position that the *Specialized Carriers* proceeding had not considered services other than private line services in determining the public interest ramifications of competition, and further indicated that it had intended to confer on A.T. & T. a monop-

<sup>36</sup> 39 FCC 2d 131.

<sup>37</sup> *Id.*, at 134, 135.

<sup>38</sup> With the Execunet service, a subscriber can reach any telephone in a distant city through the local MCI office and intercity network. Connection both locally and at the distant end is attained through the exchange telephone office in each area. None of the plant used in completing the call is dedicated to a particular customer during any specified time; rather, all of the facilities used to establish the connection are available upon demand. See *MCI v. FCC*, at 369, text and n. 3.

<sup>39</sup> *MCI v. FCC*, at 371, citing *MCI*, at 63. The letter order may be referred to in appendix B, at 62-64.

oly over MTS and WATS by that ruling, a decision which could not be changed without evidence of changed circumstances.<sup>40</sup> It expressed a similar view of the effect of its report and order in docket 19117. The Commission felt that the existing specialized carriers were allowed to offer private line services through tariff free of any prior approval requirement, but were required to proceed by section 214 applications with respect to all other services. Over MCI's objections, it concluded that Execunet was not a private line service.

On appeal, the Court analyzed the Commission's usual administrative practice of writing service restrictions in to the section 214 certificate when an individual carrier proposes to build, operate, or extend its communications lines. This procedure, specified in section 214(c), was apparently still in effect when the Commission said in docket 19117 that carriers could offer any service not restricted by certificate by simply filing a tariff. The Court observed, furthermore, that the Commission had not enacted by rulemaking any service restrictions over point-to-point microwave radio licensees as a class, and had not made its definition of "private line service" applicable to such licensees, "although this would certainly seem to be the natural thing to have done had the Commission sought to restrict specialized carriers to private line service offerings."<sup>41</sup>

It seemed to the Court that there existed no express service limitations on MCI's tariff through either of these instruments. The pivotal issues were whether and to what extent section 214 expressly allowed the Commission to impose prior approval requirements, and whether the Commission had properly exercised its section 214 authority when it rejected the Execunet tariff.

The Court stated that the primary purpose of section 214(a) is to prevent the unnecessarily duplication of facilities, not the regulation of services.<sup>42</sup>

Accordingly, it continued, as long as the "adequacy or quality" of the service set out in a certificate is not impaired by a new service introduced by tariff, in accordance with the final proviso clause in section 214(a), the public need that justified the facilities would still be met, and there is no sense in which those facilities become needlessly duplicative.<sup>43</sup>

Hence, while section 214(a) could not be used as an instrument to limit services, the Court pointed out that existing case law suggested that it was hardly possible to determine the need for a new facility under that section without considering the service to be provided over it. The Commission must impose a service restriction on the facility at the time that an application under section 214 is considered, holding itself to a strict determination of public need under section 214(c).<sup>44</sup>

In accordance with this analysis, the Court rejected the FCC's opinion that the *Specialized Common Carrier* decision restricted the services which specialized carriers could lawfully offer. Although it conceded that a service like Execunet was not under consideration

<sup>40</sup> Id., at 373, citing *MCI*, 60 FCC 2d at 56-57.

<sup>41</sup> Id., at 376.

<sup>42</sup> Id., at 377 (reference omitted).

<sup>43</sup> Id., at 378.

<sup>44</sup> Id., at 379.



during that proceeding, the rejection of that tariff was not a legitimate exercise of section 214(c) authority:

[F]ailure to consider the public interest ramifications of a service—either pro or con—during resolution of a section 214(a) application is simply not the same thing as an affirmative determination that the public convenience and necessity may require a restriction on a facility authorization limiting a carrier to provision solely of those services proposed in its section 214(a) application.<sup>45</sup>

Also, the Court's review of the *Specialized Common Carrier* decision revealed no evidence of any concern that competitive impact (revenue diversion) required restrictions on MCI's facility through section 214. Instead, it discerned an attitude in that decision that impact questions were to be resolved on a case-by-case basis through other procedures:

The undeniable import of [docket 18920] is that questions related to the future impact of specialized carrier service offerings other than those immediately at hand \* \* \* should be resolved in other proceedings—in tariff proceedings, upon license renewal, or by further rulemaking. Strikingly absent from this list is a mention of further section 214 proceedings.<sup>46</sup>

Without passing upon the merits of the Execunet offering per se, it appeared to the Court that the Commission had no general authority to insist that carriers receive its approval before filing new tariffs. Since no de jure monopoly was granted to A.T. & T. in the *Specialized Carrier* decision, no public interest conclusion could generally be drawn from the fact that another carrier's service would compete in the public message telephone field:

Only if the Commission has determined that the public convenience and necessity may require that new services receive advance approval can it then reject a tariff as unauthorized. In so holding we have not had to consider, and have not considered, whether competition like that posed by Execunet is in the public interest. That will be the question for the Commission to decide should it elect to continue these proceedings. In that eventuality the Commission must be ever mindful that, just as it is not free to create competition for competition's sake, it is not free to create monopoly for monopoly's sake.<sup>47</sup>

### *B. International common carrier*

Since the Supreme Court's decision in the *RCA* case, the FCC has granted authority for numerous direct radiotelegraph circuits, in certain instances without holding hearings. As is apparent from the Commission's disposition of that case, HF radio carriers were increasingly allowed to provide service to overseas points already served by telegraph cables. Competition existed not only between different corporate entities, but also between different point-to-point technologies; that is, different carriers used either the radio spectrum or cable.

<sup>45</sup> Id., at 380.

<sup>46</sup> Id., at 381.

<sup>47</sup> Id., at 382, citing *FCC v. RCA and Hawaiian Telephone Co. v. FCC*.

The Commission had generally followed a longstanding policy of maintaining the separation of voice and record services in the international field. Although there was no specific statutory requirement demanding this practice, it was a convenient one in that physical differences as to frequency bandwidths and methods of operation clearly distinguished each transmission mode from the other. Aside from these inherent characteristics, there existed a general policy dictate embodied in the Communications Act designed to make the antitrust laws applicable to international communications. There was always the danger that the entry of the strong voice carrier backed by almost limitless domestic resources into the international telegraph field could adversely affect the stability of the relatively much smaller competing international carriers which provided vitally important message telegraph service. There did exist a few exceptions to this dictotomy, such as the circuits in the Mainland-Hawaii cable, which had been operated by Mackay Radio to provide message telephone service.

Until the mid-1950's, facilities were wholly owned by one carrier, irrespective of its nationality. Thus, U.S. carriers were not only the sole owners of the telegraph cable and radio facilities they employed, but facility negotiations with foreign governments largely focused on the desire to secure reciprocal cable landing rights in addition to agreements concerning the division of traffic. Concomitantly, cables landed in the U.S. by foreign administrations were treated according to the terms of the Cable Landing Rights Act.

With the first of the transatlantic cable series (TAT) and the passage of the Communications Satellite Act of 1962, these distinctions began to change. In the first instance, the new variety of cable was much more sophisticated than the "old strands" built many years before, and has grown increasingly more so since that time. The practice has become to construct them as a product of bilateral negotiations. Submarine cables have evolved into joint undertakings on a divided ownership basis between a consortium of U.S. carriers and interested foreign correspondents (postal, telephone and telegraph administrations, or PTT's). Furthermore, the FCC allowed both the voice and record carriers to share cable capacity and investment, with the imposition of rate base control through section 214. This obviated competition between modes, and the voice/record distinction as well, as the carriers were allowed to engage in limited service competition over this facility. Additionally, all the American international service carriers were allowed to acquire satellite capacity, with satellite planning by COMSAT and earth station construction made subject to section 214. In order to overcome the cable bias, however, any potential competition between these two modes was qualified by a system planning mechanism. What follows is a review of the pivotal transatlantic cable authorizations and the satellite legislation which devised these section 214 requirements for the international sector.

#### 1. The first transatlantic cable decisions

- a. *American Telephone and Telegraph Co. (TAT 1)* 27 FCC 113 (1959)

TAT-1, made possible by a breakthrough in voice-grade cable technology, was laid in 1956, and represented a bilateral negotiation,

planning, and investment procedure between A.T. & T. and the British. A.T. & T. applied for licensing authority to connect its microwave facilities with the landing site, which was to be established in Canada. This was passed upon by the FCC without hearing, after having kept itself informed of the status of the TAT facility during its blueprint stages. Much the same procedure was followed for the construction of TAT-2 in 1959.

A general separation of voice from record services remained in 1956, when, during informal discussions with the British, the U.S. delegation felt it could justifiably take a position against the use of the TAT telephone facility to provide a pure telegraph service.

In April 1959, A.T. & T. applied for authority to handle both voice and record traffic over its transatlantic telephone system. Its purpose was to provide channels in the cable to transmit voice and record signals either simultaneously (SVD) or alternatively (AVD). This capacity was to fulfill a request advanced by the Department of Defense. A.T. & T. asked also that it be permitted to lease TAT-1 channels to the international record carriers for use by them in rendering telegraph or other nonvoice services. The Commission addressed the appropriate classification of the new product in a July 1, 1959 decision.

Since about the beginning of 1957, advances in the state of the art had made possible the use of very broad bands for simultaneous transmission of all types of intelligence through conversion to basic impulses indistinguishable from each other. In addition, demands had increased, particularly from the defense community, for the provision, from discrete facilities, of alternative transmission service. Voice-grade circuits could be used for record transmission; and they could be subdivided into a number of telegraph-type circuits for use in the provision of telegraph message service and telex. The nature and rapidity of these changes had begun to obviate the distinction between voice and record. Therefore, the Commission decided that there was no longer any reason, on the basis of physical facilities or service needs, to maintain the separation for military requirements.

This judgment produced a dilemma during its concurrent review of the proposal to lease channels to the international record carriers. The record carriers had reacted favorably to A.T. & T.'s initiative of requesting lease authority. However, certain of them, including Western Union and the American Cable and Radio Group (A.C. & R., the holding company for ITT subsidiaries), had stressed that any authorization should permit them to furnish AVD/SVD for defense purposes, as well as strictly nonvoice services, so that they could compete with A.T. & T. on an equal basis for defense agency communication business. A.T. & T. on the other hand, complained that it should not be induced to enable competitors to use its own facilities to compete with it. The Commission ultimately felt that it should not risk impairing the financial stability of the IRC's through any diversion of revenues that might result from a grant of A.T. & T.'s application. It therefore approved the leasing of the TAT facility to the IRC's, stipulating that the lease may be used to provide AVD/SVD service to the defense community in addition to the provision of record service to all users. The IRC's initially leased cable circuits from A.T. & T. and later acquired them on an indefeasible right of



user basis (IRU), which transferred that investment from the A.T. & T. to the IRC rate bases.

The TAT-1 facility became the vehicle for a significant departure from established practice. Not only did it initiate the bilateral ownership and investment option, it also created a precedent for allowing carriers that had traditionally been limited to one medium—radio—to collectively use, if not yet invest in or own, the alternative cable technology.<sup>48</sup>

This was impelled by the evidence that state-of-the-art advancements had made possible the transmission of both voice and record over the same facility; and that there existed no need to separate voice and record communications for specialized requirements. Thus, a single action upset both the voice/record and radio/cable dichotomies.

Although the lease proceeding deliberated over a microwave radio license, it did involve a refinement of a certification standard, one that was voiced in the 1936 *Oslo Circuits* case: that the authorized service not result in undue market diversion from competing carriers. There had traditionally been no explicit concern for the implications of rate base regulation for duplications of international routes, and this was still the case. The interest in the lease action existed not in terms of the facility itself, since A.T. & T. had already absorbed the investment risk, but in terms of the service to be provided over that facility. As an innovation that A.T. & T. wished to retain exclusively, AVD/SVD posed a threat to the military business conducted by the other carriers. The Commission was obligated to assess this possibility, and compromised by allowing the IRC's to offer the service in conjunction with A.T. & T.

b. *American Telephone and Telegraph Co., et al.* (TAT-4) 37 FCC 1151 (1964)

The economic viability of the IRC's and the services which they provide remained uppermost in the Commission's criteria of permissible service entry, and the issue returned in the context of the TAT-4 proceeding in 1964. By this stage, the Commission had begun requiring section 214 authorizations prior to the construction of transoceanic cables that landed in the United States. An application to construct was generally considered in conjunction with an application for a cable landing license. It was reasoned if the carriers were to claim these sophisticated and costly capital investments as rate base components, they should then be subject to qualifiable review in order to prevent unremunerative risks which the routinely guaranteed return compensation process might not ordinarily discern or prevent. The Commission had also begun to expressly apply the section 214 obligation to leases requested on an IRU basis, since they were to be treated as investments for ratemaking purposes.

The TAT-4 rulemaking acted on A.T. & T.'s application, submitted pursuant to section 214, to construct a cable between the United States and France. Consolidated with the proceeding was an additional request from that carrier that its microwave licenses and section 214

<sup>48</sup> This leasing practice was followed in order to apply the relatively sophisticated cable capacity to user requirements that could not be fulfilled by radio telegraph. *Commercial Cable Co.*, 28 FCC 283, 293 (1960), citing *A.C. & R., et al.*, proceeding of Feb. 17, 1960.

certificate be amended to allow it to offer AVD service to all customers over its TAT-3 facility. The Commission discovered that A.T. & T. was providing all the AVD/SVD circuits leased by DOD. It decided that, to prevent economic harm to the IRC's, and to guarantee the continuance of their services, only these entities would be authorized to furnish leased AVD/SVD circuits in the future.

TAT-4 also allowed the IRC's to become joint owners of submarine cables which would provide them with a voice in management and operation that was not forthcoming from IRU acquisition. Ownership would be shifted upon Commission approval of applications filed for a cable landing license and for certification under section 214.

Additionally, the Commission took advantage of the rulemaking opportunity to extend its certification power over equipment that derives international channels of communication. Its action was similar to the jurisdiction asserted in 1938 over domestic carrier-type equipment:

A.T. & T. and the various record carriers have increased the capacity of, or the number of messages (voice and record) handled by their respective facilities by the use of appropriate equipment; for example, the use of Time Assignment Speech Interpolation (TASI) equipment by A.T. & T. To date, we have not exercised the authority given us pursuant to the provisions of section 214 of the act to require the filing and a grant of appropriate applications before installation of such equipment. We feel, however, that, in view of the rapid growth of facilities in this field, the imminence of satellite communications, and the vast increase in facilities possible through heretofore unregulated installations, we should require such an application and a grant thereof before the installation of such equipment. Accordingly, we propose to set forth in the authorization to be granted pursuant to section 214 of the act for this new cable the condition that TASI, or any other equipment designed to increase the number of voice or record channels derived from, or utilized in, such cable, shall not be increased by A.T. & T., or any other carrier until appropriate authorization pursuant to section 214 of the act is sought and obtained from this Commission.<sup>49</sup>

During the TAT-4 negotiations, the Communications Satellite Act was passed: the next submarine cable, TAT-5, was proposed after the initiation of satellite service.

## *2. The global satellite legislation*

The Communications Satellite Act of 1962<sup>50</sup> was passed in anticipation of U.S. membership in INTELSAT, an international consortium of countries established to plan, own, and operate the space segment of an international communications system. The act established the Communications Satellite Corporation (COMSAT) as the U.S. entity authorized to participate in the ownership and operation of INTELSAT satellites. It also set forth a national policy that a

<sup>49</sup> TAT 4, at 1158.

<sup>50</sup> Act of Aug. 13, 1962, 47 U.S.C. 701 et seq.

commercial communications satellite system be established "as expeditiously as practicable" and "as part of an improved global communications network," in conjunction and cooperation with other countries. These new communications services were to be made available "as promptly as possible and . . . extended to provide global coverage at the earliest possible date."<sup>51</sup> The President and the FCC were given responsibilities to implement this policy under title II of the act.

The President was to coordinate the activities of governmental agencies with responsibilities in the field of telecommunications "so as to insure that there is full and effective compliance at all times with the policies set forth" in the act.<sup>52</sup> He also was given the authority to exercise supervision over relationships of COMSAT with foreign governments or international bodies "as may be appropriate to assure that such relationships shall be consistent with the national interest and foreign policy of the United States."<sup>53</sup> These functions were subsequently delegated by Executive Order No. 11191. His responsibilities over COMSAT and over the telecommunications agencies were given to the Department of State and to the Executive Office of Telecommunications Policy respectively. (In April 1978, OTP became part of the National Telecommunications and Information Agency in the Department of Commerce).

The COMSAT Act directed the Commission to "insure effective competition \* \* \* in the procurement by the corporation (COMSAT) and communications common carriers of apparatus, equipment, and services required for the establishment and operation of the communications satellite system and satellite terminal stations."<sup>54</sup> COMSAT was defined as a "common carrier" within the meaning of the Communications Act of 1934, and it was explicitly made "fully subject" to titles II and III of that act.<sup>55</sup> The COMSAT Act also gave broad authority to the Commission over construction: its mandate was to "grant appropriate authorizations for the construction and operation of each satellite terminal station, either to the corporation or to one or more authorized carriers or to the corporation and one or more such carriers jointly, as will best serve the public interest, convenience and necessity."<sup>56</sup> The construction of satellite earth stations, as well as COMSAT's participation with INTELSAT in the construction of satellites, were made subject to the standards of section 214:

[The Federal Communications Commission . . . shall] require, in accordance with the procedural requirements of section 214 of this title, that additions be made by the corporation or carrier with respect to facilities of the system or satellite terminal stations where such additions would serve the public interest, convenience, and necessity[.]<sup>57</sup>

<sup>51</sup> Id., at 701(a)(b).

<sup>52</sup> Id., at 721(a)(3).

<sup>53</sup> Id., at 721(a)(4).

<sup>54</sup> Id., at 721(c)(1).

<sup>55</sup> Id., at 741.

<sup>56</sup> Id., at 721(c)(7).

<sup>57</sup> Id., at 721(c)(10).



### *3. The system planning concept*

The Commission's review of ATT's TAT-5 proposal differed from earlier authorization proceedings in two respects. First, as a matter of circumstance, the Commission was faced with the need to consider the comparative operational and cost advantages of alternative technologies—satellite and cable—and to decide which of these, or what combination of both, would best serve the public interest.<sup>58</sup> Second, the FCC enacted certain procedural changes for the cable project in order to systematically evaluate this new planning element.

The satellite/cable dichotomy embodies the contrasting planning processes and objectives for the different modes, and the respective proprietary interests on the part of the particular countries negotiating communications links with each other. Cable projects are bilateral operations which constitute commitments between a number of U.S. carriers and foreign entities. This arrangement fulfills anticipated communications needs over one international traffic path. In contrast, satellite facilities are commonly owned by all members of Intelsat, with the objective of developing communications availability on a global basis. Some administrations prefer the greater proprietary control deriving from cable ownership. In addition, there are varying capacities among nations for the manufacture of cable and satellite facilities, as well as different social and political objectives which may affect each country's preference of cable and satellite facilities. Finally, preferences for cable or satellites are affected by the various operational viewpoints about the cost, reliability, and performance of either medium.

In order to exercise its prerogative to control the various elements of the ICC's investment decisions, the Commission imposed a new procedure upon the negotiations for TAT-5. Previously, the IRC's had reached agreement with the European PTT's and then submitted the contract for Commission approval. In this instance, the carriers were requested to refrain from reaching a final agreement until further Commission consideration of the project. The agency addressed the question of the proper utilization of cable and satellite facilities in order to fulfill the established U.S. policy favoring the earliest possible implementation of a global satellite communications system.

After requesting and receiving considerable data concerning the proposed cable, the Commission concluded that the TAT-5 applicants should hold themselves to a "proportionate fill" criterion:

[The section 214 application should show] that the entities (the U.S. carriers and foreign PTT's) owning the cable or having indefeasible rights of user therein have agreed to use satellite circuits for the handling of traffic in numbers sufficient to assure that this cable and the satellite facilities provided to handle traffic between the United States and their respective countries shall each be filled at the same proportionate rate.

By proportionate fill we mean that the unfilled capacity of the satellites shall be leased at a rate (with appropriate adjustments), so that, when added to the use made by other entities who do not use TAT-5, unused satellite capacity is

<sup>58</sup> U.S. House, *Report by the Federal Communications Comm.*, op. cit., IV, n. 1, p. 429.

leased by all users at the same rate as the cable is filled to the end that both types of facilities reach the 100-percent fill figure at approximately the same time.<sup>59</sup>

Moreover, to insure that the cable and satellite facilities would in fact be used in the manner authorized, the Commission withheld permission to activate circuits in the new cable, requiring a separate application for activation authority. The proportionate fill and circuit-by-circuit activation requirements constituted the Commission's first effort at fulfilling its mandate to assure that the newer and potentially cheaper satellite technology would be utilized by carriers whose principal economic and operational interests lay with the older cable technology.<sup>60</sup>

This attempt at system optimization was a significant departure from past FCC procedure. As we have seen, the Commission's first years of reluctance to allow duplicating international service was transformed to an opposite endorsement of competition. After litigation, this disposition was clearly qualified to the effect that a generalized "national policy" of competition had to be supplemented in each instance by a reasonably confident forecast of feasibility and benefit. There had to exist demand sufficient to support competition; and there had to exist a probability that a positive effect would result on service and rates. Aside from license renewal at regular intervals and the receipt of route-by-route statistical data, the Commission's involvement generally ended when the outcome of a licensing proceeding was announced; and the carrier was generally free to attract whatever business it could.

The purpose of this effort was very close to one of the two joint objectives of section 214. The Commission was obligated to prevent service deterioration that might result from such competitive market diversion as might cause one or more other entities to fail. When the Commission did apply section 214 requirements to international transmission facilities, it used not only this rationale, but also that statute's associated purpose; i.e., the exercise of a veto power to discourage rate base inflation. Never did it devise a planning scheme to qualify the utilization of one medium with another. That is to say, never were explicit policy restrictions placed on cable in reference to radio or vice versa. In the 1930's, the Commission discouraged duplication irrespective of the medium in question in any particular hearing. Its reverse policy was followed in the same fashion; and the benefit accrued to the radio medium since few cable landing licenses were requested.

The FCC's policy of encouraging satellite potential was analogous in purpose to the confrontation by its predecessor of the novel radio technology. However, the disposition of the radio agency to encourage the establishment and entry of radio carriers did not countenance a "quota" mechanism; nor could it (as a matter of jurisdiction) confine the cable carriers from their initiative to compete for additional routes. Its methodology was to insure the independent development of radio, and its evasion from the dominance of the established cable technology. The new satellite technology, in contrast, though "glamo-

<sup>59</sup> *A.T. & T./TAT-5 project*, 11 FCC 2d 957, 958 (1968).

<sup>60</sup> U.S. House, op. cit., n. 58, p. 432.

rous", was relatively expensive and required an affirmative commitment to develop its global potential and to ultimately achieve its inherent long-run economies. The instinct on the part of the carriers was to maintain ownership in cable, not only because it was demonstrated and familiar, but also because satellite transmission represented an investment risk. Satellite planning through COMSAT was made subject to authorization under section 214. Therefore, the carriers were to procure this capacity through lease, with only earth station construction to provide a return as a rate base investment (and hence subject to control under section 214). The preference for cable hindered both the growth of a competitive global satellite system alternative and the efficient use of communications facilities. The FCC's conditional stipulation on cable fill was an effort to overcome this impediment to its statutory mandate. This response, however, constituted a freeze on the market share between cable and satellite, and thus created conflicts with the carriers' foreign correspondents. Also, the creation of divided authorities in the Satellite Act created administrative confusion with respect to facilities commitments.

These divided authorities—the FCC's obligation to interact with the Department of State and OTP pursuant to the provisions of the COMSAT Act and Executive Order No. 11191—gave rise to a disagreement between the FCC and the Department of State concerning their respective obligations. The State Department felt that the act gave the President or his delegate the authority to make the final determination on government instructions to COMSAT. The FCC took the position that it was to be the final authority on facilities matters. The FCC argued that its powers under section 721(c) were not intended by Congress to be subject to any review by another government agency. While it agreed that "foreign relations" and "national policy" must be taken into account in determining instruction to COMSAT, it felt that this obligation must be conducted with the advice of the State Department and other relevant agencies, in the course of its determination pursuant to section 721(c). It took the position that, if a section 721(c) issue arrived on the stage of a public hearing, foreign policy interests would be subsidiary to the narrow statutory test of the "public interest"; the Department of State countered that the public interest might itself be subsidiary to the national interest of the United States as defined in section 721(a).<sup>61</sup>

This disagreement brought about a statement, developed in August 1966 by the State Department and approved by the relevant agencies, which established procedures for sending coordinated, lucid instructions to COMSTAT.<sup>62</sup> However, the instructional process was intentionally left vague, and the issue of who was in charge of instructing COMSAT has never since been resolved.<sup>63</sup>

<sup>61</sup> U.S. General Accounting Office, Report by the Comptroller General to the House of Representatives, *International Telecommunications Facilities* (1978), p. 38.

<sup>62</sup> *Loc. cit.*; see appendix V.

<sup>63</sup> *Id.*, p. 39 (reference omitted).



## VI. SUMMARY

### *II. Section 214 of the Transportation Act of 1920*

A precursor of the certification requirement for common carriers operating in interstate commerce existed in some States during the early nineteenth century as a condition of grants of railroad charters. As the Nation expanded in size and density, the States allowed railroads to develop where they could. Regional and local corporations constructed facilities and established service with substantial public assistance and patronage.

The Interstate Commerce Act of 1887 created the Interstate Commerce Commission and the first direct Federal control over the industry's rates and conditions of service. The act prohibited pooling arrangements in order to control railroad monopoly, discouraging the systematic planning of construction. As did most existing State law, the ICA neglected the issue of facilities duplication.

The 1887 act was amended by the Transportation Act of 1920, the outcome of a comprehensive congressional review of regulatory policy. The Transportation Act emphasized the efficient, systematic, and less restrictive management of industry structure. As part of this scheme, the construction, extension, or abandonment of railroad lines was made subject to ICC review. Common carriers were to apply for and receive a certificate of public interest, convenience, and necessity in order to construct, extend, or abandon a line. This enactment preceded a detailed and extensive history of the same regulatory obligation in the communications industry.

It had become obvious by this time that the competitive tradition of the railroad industry, and the regulation that had been imposed on it, encouraged speculation and poor management. Instability resulted from construction and extensions into sparsely populated territory or parallel to already adequate routes. Abandonment of unremunerative lines disregarded the needs of communities which had come to rely on the service. Consequently, the purpose of section I(18)-(22) of the Interstate Commerce Act was to regulate direct, duplicative competition and to control rate base valuation through its reach on investment. An authorization for the ICC to compel the provision of facilities or extensions of lines was contained in section I(21). However, paragraph 21 was weakened by the Supreme Court in *ICC v. Oregon-Washington Railroad and Navigation Co.*, and the issue has never been relitigated.

The ultimate benefit of section I(18)-(22) was to redound to the public in the form of cost savings and of the reinforcement of the common carrier obligation through the guarantee of service. This check on management would presumably also establish an incentive for outside sources to extend investment capital and credit to the rail system. By the time the Communications Act was enacted, these goals were reiterated in several Supreme Court interpretations of the statute.

### *III. The communications version of section I(18)-(22)*

As is the purpose of the retrospective discussion of the railroad business, section III reviews the development of communications in order to provide an understanding of its status as an industry when given regulatory treatment. The development of end-to-end service and of the nationally coordinated network was underway early in the century. Through the next several years, interstate toll service was effected through a relatively rudimentary system of direct lines between exchanges and manual switches. By the passage of the Communications Act of 1934, a general toll switching plan introduced efficiencies that formed the basis for today's integrated system of automatic switching among toll offices and the indirect trunk groups.

This network was devised and implemented by the sole-source provider of telephone service, as the logical outgrowth of State public utility regulation and of the concept of natural monopoly. The number of service offerors was restricted to one for each geographic area through franchise and certification, a direct forerunner of the rationale of section 214. Telephone and telegraph companies were entered into the Interstate Commerce Act in 1910 and through amendments attached to the Transportation Act of 1920. An antitrust exemption was granted in 1921 to telephone company consolidations. All of this insured a common carrier obligation on the monopoly provider of voice telephone service, but had very marginal effect on international transmission.

The Radio Act of 1927 addressed the need to encourage a transoceanic radiotelegraph service independent from and competing with the cable medium. That act applied the antitrust laws to the manufacture and sale of radio facilities and to the ownership of the newly developing technology by the cable carriers. The Radio Commission developed a practice of authorizing as many requests for instituting service as were feasible, i.e., to every point where enough traffic existed to support new entry, resulting in substantial competition and facilities duplication.

The Communications Act of 1934 was based on both the Interstate Commerce Act and the Radio Act. Its overall intent was to create the Federal Communications Commission so as to centralize jurisdiction over the diverse communications industries. It is evident that the act was drawn from existing laws with little substantive change in language or existing intent. The legislative authority for direct, duplicative competition in the international sector was transplanted into title III in the form of section 314. Section 214(a)-(d) derived from section I(18)-(22) of the Interstate Commerce Act, and with the same controlling goals, i.e., as a check on interstate investment and competition.

### *IV. The formation of policy*

Section 214 was amended in 1943, during the enactment of section 222, to clarify its application to the merged telegraph industry. A certification requirement was added for abandonment of service, as was contained in section I(18) of the Interstate Commerce Act. The term "line" was defined very broadly as "any channel of communication established by the use of appropriate equipment . . ." The term had been the lynchpin of the FCC's administration of section 214; and the



amendment was a policy choice over the industry's definition, which would have limited the term to physical wires on poles.

The Commission had been attempting to establish its jurisdiction under the language of section 214. The issues of entry regulation and rate base control in the domestic sector actually devolved on interpreting the imprecise and vague language to find the breadth and limit of control over carrier action. It was ultimately settled that the corporate obligation to apply for and receive a certificate encompassed several methods of construction, extension, or acquisition of "lines." The rulings in *Mackay Radio and Telegraph Co.* and *Southwestern Bell Telephone Co.* determined, respectively, that the acquisition of new circuits by lease, and the establishment through switches of an interstate toll capability were both tantamount to the establishment of a new interstate "channel of communication." This definition applied liability to section 214 even though in the former instance, the subject carrier did not own the line involved, and in the latter, intrastate traffic amounted to 90 percent of channel utilization. This jurisdiction was broadened in 1944 to include the addition of extra transmission capacity on existing facilities; the outcome of *American Telephone and Telegraph Co.* was to construe such action as the addition of "lines."

The industry contested this broad determination, preferring to give the term "line" the meaning of simple wires. During these first years, however, technical innovation had become a fairly intrinsic characteristic of the industry which the FCC observed and on which it had to apply its legislative directives. There had developed several means through which market entry and additions of cost could be accomplished. Therefore, it seemed obvious to the Commission that it must control the acquisition of circuitry and other elements not mentioned in the statute and barely treated in prior case law.

The international record carriers utilized either the cable or the radio mode, the operating requirements and facilities of which were technologically more "cooperative" with the Communications Act than were the circuit utilization issues in the domestic sector. Since the act did not treat cable landing authorizations, the Commission was obligated to handle only radio construction permits and licenses under title III. This activity, and its legislative underpinnings, were directly inherited from the Radio Commission; an administrative sanction of liberal entry into the international sector was relatively straightforward.

This policy choice was qualified by the FCC in the *Oslo Circuits* case with a stringent requirement that competitive entry fulfill some public benefit through service improvement; and this reasoning was affirmed on judicial appeal.

The Commission continued denying title II requests for competing international service until after World War II. At that time, as illustrated by the *Bermuda Circuits* case, the agency began to return to a policy of encouraging competition. The Supreme Court's resolution in 1953 of the *Three Circuits* controversy established a modicum of administrative guidance on this policy trend. It said in *FCC v. RCA Communications* that the Commission must exert an affirmative judgment of market need in entry control rulings, rather than authorizations of competition for competition's sake. While a detailed forecast of specifics was not necessary, the Court's standard was for the FCC to



test the evidence for a probability that competition would fulfill some demand and would generally result in public benefit. This ruling became a precedent for general reference to the issues of market entry and facilities duplication in the telecommunications industry.

#### *V. The implementation of policy*

Section V discerns the translation of legislative intent and tested administrative practice to policy methods that have been recently devised to regulate facility investment and market entry into domestic and international telecommunications.

Advances in sophistication and scale of the nationwide voice network have complicated the FCC's task of controlling facility additions to the interstate rate base. This is illustrated by a brief digression on the characteristics of the nationwide delivery system and the service standards by which it is administered. This provides the framework for a review of the FCC's attempt in docket 19129 to audit network costs as a major rate base element.

State jurisdiction remains controlling at a less comprehensive scale, over local exchange investment designed to benefit purely local or intrastate service. Since local distribution facilities may be engineered to broadband capacity, they may also serve cable television systems as well as exchange connections. However, the telephone company's involvement in the local cable network is subject to the Commission as a common carrier function. In *General Telephone Company of California*, local exchange companies were made liable to section 214 certification prior to supplying facilities to CATV operations. The FCC construed this service within the context of its ruling in *Southwestern Bell Telephone Co.*, as an interstate channel of communications when carrying television signals.

In addition to these two pivotal rate base control rulings, section V also reviews the traits of the domestic data communications industry that attracted new entry and induced the Commission to enact a change in market structure to liberalize the delivery of specialized telecommunications services. The *Specialized Common Carrier Services* decision is emphasized as the agency's test of the probable results of open entry and competition. The prospect of economic impact was assessed as a section 214 entry question, and the evidence of public need was analysed to suit the standard of *FCC v. RCA*. The FCC said essentially that the record indicated the existence of a market that was growing rapidly, was not related to traditional telephone service, and needed no large capital investment to deliver service. This satisfied the Commission that open entry was possible and would fulfill a public need.

Section 214 certification was made necessary for specialized carrier facilities because they create "channels of communication" through their own lines. The open entry philosophy was broadened to permit resale and sharing arrangements in a separate ruling. Resellers were made subject to section 214 because they serve for a profit through channels acquired by lease, and the FCC based this jurisdiction on its very early reasoning in *Mackay Radio*.

The FCC regarded the scope of the *Specialized Common Carrier* policy as limited exclusively to the offering of customized private line services by the specialized carriers, with MTS and WATS equivalents reserved to the general service carriers. This stance was expressed in

determining the status of a class of service offered by MCI Telecommunications Corp. The Commission determined that the *Specialized Common Carrier* decision and MCI's section 214 authorizations had limited its facility to the provision of essentially private line service, and that its Execunet tariff was the marketing of a functionally similar service to switched message telephone. The Execunet tariff was terminated as an unlawful service.

On review, the District of Columbia Circuit Court dismissed the action, saying that the Commission had not held to the prior approval requirements of section 214(c). Furthermore, the court held that the *Specialized Common Carrier* decision had not definitively precluded entry into areas that were not technically private line markets.

There was a resurgence of utilizing cable technology for international communications in the 1950's; and A.T. & T. initiated the first of the bilaterally owned transatlantic series. Section 214 applications were made necessary for the first time in authorizations of international service, in the context of TAT cable construction. The reason for this is that cables were viewed as investment risks for rate base purposes. While they were at first operated for strictly voice telephone service, the Commission shortly began to permit acquisition of cable capacity by the record carriers. Since this mode could cater to more sophisticated requirements than could radiotelegraph, it was felt that its exclusive use by one carrier would have the effect of competitive market entry. Indefeasible right of user (IRU) arrangements negotiated by the record carriers were to be treated as investments for rate-making purposes. Therefore, these acquisitions were also made subject to the section 214 application and review requirements.

In creating the Communications Satellite Corporation (COMSAT), the Communications Satellite Act of 1962 gave it common carrier status, and held it to the requirements of section 214. The COMSAT Act gave the FCC the broad authority to review both satellite earth station construction and the Corporation's space segment procurement plans, and to maintain competition between the carriers in the procurement of satellite capacity. Supervisory authority was also delegated to the Department of State and the Executive Office of Telecommunications Policy for national interest and foreign policy reasons.

In order to control the effect of TAT cable construction on satellite utilization, the Commission instituted stringent criteria on the certification process. This was to insure that the carriers would not neglect the novel satellite capacity. This objective persists to this day, obviating competition between modes. In conjunction with the creation of divided authorities in the Satellite Act, it also has created some confusion with respect to facilities commitments.



## APPENDIX

### A. SECTION I(18)-(22) OF INTERSTATE COMMERCE ACT OF 1887, PER AMENDMENT BY TRANSPORTATION ACT OF 1920

(18) After ninety days after this paragraph takes effect no carrier by railroad subject to this Act shall undertake the extension of its line of railroad, or the construction of a new line of railroad, or shall acquire or operate any line of railroad, or extension thereof, or shall engage in transportation under this Act over or by means of such additional or extended line of railroad, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require the construction, or operation, or construction and operation, of such additional or the operation thereof, is proposed to be abandoned, with the right to be heard abandon all or any portion of a line of railroad, or the operation thereof, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity permit of such abandonment.

(19) The application for and issuance of any such certificate shall be under such rules and regulations as to hearings and other matters as the Commission may from time to time prescribe, and the provisions of this Act shall apply to all such proceedings. Upon receipt of any application for such certificate the Commission shall cause notice thereof to be given to and a copy filed with the governor of each State in which such additional or extended line of railroad is proposed to be constructed or operated, or all or any portion of a line of railroad, or the operation thereof, is proposed to be abandoned, with the right to be heard as hereinafter provided with respect to the hearing of complaints or the issuance of securities; and said notice shall also be published for three consecutive weeks in some newspaper of general circulation in each county in or through which said line of railroad is constructed or operates.

(20) The Commission shall have power to issue such certificate as prayed for, or to refuse to issue it, or to issue it for a portion or portions of a line of railroad, or extension thereof, described in the application, or for the partial exercise only of such right or privilege, and may attach to the issuance of the certificate such terms and conditions as in its judgment the public convenience and necessity may require. From and after issuance of such certificate, and not before, the carrier by railroad may, without securing approval other than such certificate, comply with the terms and conditions contained in or attached to the issuance of such certificate and proceed with the construction, operation, or abandonment covered thereby. Any construction, operation, or abandonment contrary to the provisions of this paragraph or of paragraph (18) or (19) of this section may be enjoined by any court of competent jurisdiction at the suit of the United States, the Commission, any commission or regulating body of the State or States affected, or any party in interest; and any carrier which, or any director, officer, receiver, operating trustee, lessee, agent, or person, acting for or employed by such carrier, who knowingly authorizes, consents to, or permits any violation of the provisions of this paragraph or of paragraph (18) of this section, shall upon conviction thereof be punished by a fine of not more than \$5,000 or by imprisonment for not more than three years, or both.

(21) The Commission may, after hearing, in a proceeding upon complaint or upon its own initiative without complaint, authorize or require by order any carrier by railroad subject to this Act, party to such proceeding, to provide itself with safe and adequate facilities for performing as a common carrier its car service as that term is used in this Act, and to extend its line or lines: *Provided*, That no such authorization or order shall be made unless the Commission finds,



as to such extension, that it is reasonably required in the interest of public convenience and necessity, or as to such extension or facilities that the expense involved therein will not impair the ability of the carrier to perform its duty to the public. Any carrier subject to this Act which refuses or neglects to comply with any order of the Commission made in pursuance of this paragraph shall be liable to a penalty of \$100 for each day during which such refusal or neglect continues, which shall accrue to the United States and may be recovered in a civil action brought by the United States.

(22) The authority of the Commission conferred by paragraphs (18) to (21), both inclusive, shall not extend to the construction or abandonment of spur, industrial, team, switching or side tracks, located or to be located wholly within one State, or of street, suburban, or interurban electric railways, which are not operated as a part or parts of a general steam railroad system of transportation.

## B. COMMUNICATIONS ACT OF 1934

### 1. SECTION 214 (A)-(D)

#### *Extension of lines*

SEC. 214. (a) No carrier shall undertake the construction of a new line or of an extension of any line, or shall acquire or operate any line, or extension thereof, or shall engage in transmission over or by means of such additional or extended line, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require the construction, or operation, or construction and operation, of such additional or extended line: *Provided*, That no such certificate shall be required under this section for the construction, acquisition, operation, or extension of (1) a line within a single State unless said line constitutes part of an interstate line, (2) local, branch, or terminal lines not exceeding ten miles in length, or (3) any lines acquired under section 221 of this Act: *Provided further*, That the Commission may, upon appropriate request being made, authorize temporary or emergency service, or the supplementing of existing facilities, without regard to the provisions of this section.

(b) Upon receipt of an application for any such certificate the Commission shall cause notice thereof to be given to and a copy filed with the Governor of each State in which such additional or extended line is proposed to be constructed or operated, with the right to be heard as provided with respect to the hearing of complaints; and the Commission may require such published notice as it shall determine.

(c) The Commission shall have power to issue such certificate as prayed for, or to refuse to issue it, or to issue it for a portion or portions of a line, or extension thereof, described in the application, or for the partial exercise only of such right or privilege, and may attach to the issuance of the certificate such terms and conditions as in its judgment the public convenience and necessity may require. After issuance of such certificate, and not before, the carrier may, without securing approval other than such certificate, comply with the terms and conditions contained in or attached to the issuance of such certificate and proceed with the construction, acquisition, operation, or extension covered thereby. Any construction, acquisition, operation, or extension contrary to the provisions of this section may be enjoined by any court of competent jurisdiction at the suit of the United States, the Commission, the State commission, any State affected, or any party in interest.

(d) The Commission may, after full opportunity for hearing, in a proceeding upon complaint or upon its own initiative without complaint, authorize or require by order any carrier, party to such proceeding, to provide itself with adequate facilities for performing its service as a common carrier and to extend its line; but no such authorization or order shall be made unless the Commission finds, as to such extension, that it is reasonably required in the interest of public convenience and necessity, or as to such extension or facilities that the expense involved therein will not impair the ability of the carrier to perform its duty to the public. Any carrier which refuses or neglects to comply with any order of the Commission made in pursuance of this paragraph shall forfeit to the United States \$100 for each day during which such refusal or neglect continues.

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Source: ch. 652, 48 Stat. L. 1075-76 (1934).

## 2. SECTIONS 313, 314

### *Application of antitrust laws*

SEC. 313. All laws of the United States relating to unlawful restraints and monopolies and to combinations, contracts, or agreements in restraint of trade are hereby declared to be applicable to the manufacture and sale of and to trade in radio apparatus and devices entering into or affecting interstate or foreign commerce and to interstate or foreign radio communications. Whenever in any suit, action, or proceeding, civil or criminal, brought under the provisions of any of said laws or in any proceedings brought to enforce or to review findings and orders of the Federal Trade Commission or other governmental agency in respect of any matters as to which said Commission or other governmental agency is by law authorized to act, any licensee shall be found guilty of the violation of the provisions of such laws or any of them, the court, in addition to the penalties imposed by said laws, may adjudge, order, and/or decree that the license of such licensee shall, as of the date of the decree or judgment becomes finally effective or as of such other date as the said decree shall fix, be revoked and that all rights under such license shall thereupon cease: *Provided, however,* That such licensee shall have the same right of appeal or review as is provided by law in respect of other decrees and judgments of said court.

### *Preservation of competition in commerce*

SEC. 314. After the effective date of this Act no person engaged directly, or indirectly through any person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such person, or through an agent, or otherwise, in the business of transmitting and/or receiving for hire energy, communications, or signals by radio in accordance with the terms of the license issued under this Act, shall by purchase, lease, construction, or otherwise, directly or indirectly, acquire, own, control, or operate any cable or wire telegraph or telephone line or system between any place in any State, Territory, or possession of the United States or in the District of Columbia, and any place in any foreign country, or shall acquire, own, or control any part of the stock or other capital share or any interest in the physical property and/or other assets of any such cable, wire, telegraph, or telephone line or system, if in either case the purpose is and/or the effect thereof may be to substantially lessen competition or to restrain commerce between any place in any State, Territory, or possession of the United States, or in the District of Columbia, and any place in any foreign country, or unlawfully to create monopoly in any line of commerce; nor shall any person engaged directly, or indirectly through any person directly or indirectly controlling or controlled by, or under direct or indirect common control with, such person, or through an agent, or otherwise, in the business of transmitting and/or receiving for hire messages by any cable, wire, telegraph, or telephone line or system (a) between any place in any State, Territory, or possession of the United States, or in the District of Columbia, and any place in any other State, Territory, or possession of the United States; or (b) between any place in any State, Territory, or possession of the United States, or the District of Columbia, and any place in any foreign country, by purchase, lease, construction, or otherwise, directly or indirectly acquire, own, control, or operate any station or the apparatus therein, or any system for transmitting and/or receiving radio communications or signals between any place in any State, Territory, or possession of the United States, or in the District of Columbia, and any place in any foreign country, or shall acquire, own, or control any part of the stock or other capital share or any interest in the physical property and/or other assets of any such radio station, apparatus, or system, if in either case the purpose is and/or the effect thereof may be to substantially lessen competition or to restrain commerce between any place in any State, Territory, or possession of the United States, or in the District of Columbia, and any place in any foreign country, or unlawfully to create monopoly in any line of commerce.

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Source : Ch. 652, 48 Stat. L. 1087-88 (1934).



### 3. SECTION 214, PER COMMUNICATIONS ACT AMENDMENTS OF 1943

SEC. 2. Section 214 (a) of the Communications Act of 1934, as amended, is hereby amended to read as follows:

"SEC. 214. (a) No carrier shall undertake the construction of a new line or of an extension of any line, or shall acquire or operate any line, or extension thereof, or shall engage in transmission over or by means of such additional or extended line, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require the construction, or operation, or construction and operation, of such additional or extended line: *Provided*, That no such certificate shall be required under this section for the construction, acquisition, or operation of (1) a line within a single State unless such line constitutes part of an interstate line, (2) local, branch, or terminal lines not exceeding ten miles in length, or (3) any line acquired under section 221 or 222 of this Act: *Provided further*, That the Commission may, upon appropriate request being made, authorize temporary or emergency service, or the supplementing of existing facilities, without regard to the provisions of this section. No carrier shall discontinue, reduce, or impair service to a community, or part of a community, unless and until there shall first have been obtained from the Commission a certificate that neither the present nor future public convenience and necessity will be adversely affected thereby; except that the Commission may, upon appropriate request being made, authorize temporary or emergency discontinuance, reduction, or impairment of service, or partial discontinuance, reduction, or impairment of service, without regard to the provisions of this section. As used in this section the term 'line' means any channel of communication established by the use of appropriate equipment, other than a channel of communication established by the interconnection of two or more existing channels: *Provided, however*, That nothing in this section shall be construed to require a certificate or other authorization from the Commission for any installation, replacement, or other changes in plant, operation, or equipment, other than new construction, which will not impair the adequacy or quality of service provided."

SEC. 3. Section 214 (b) of the Communications Act of 1934, as amended, is hereby amended to read as follows:

"(b) Upon receipt of an application for any such certificate, the Commission shall cause notice thereof to be given to, and shall cause a copy of such application to be filed with, the Secretary of War, the Secretary of the Navy, and the Governor of each State in which such line is proposed to be constructed, extended, acquired, or operated, or in which such discontinuance, reduction, or impairment of service is proposed, with the right to those notified to be heard; and the Commission may require such published notice as it shall determine."

SEC. 4. Section 214 (c) of the Communications Act of 1934, as amended, is hereby amended to read as follows:

"(c) The Commission shall have power to issue such certificate as applied for, or to refuse to issue it, or to issue it for a portion or portions of a line, or extension thereof, or discontinuance, reduction, or impairment of service, described in the application, or for the partial exercise only of such right or privilege, and may attach to the issuance of the certificate such terms and conditions as in its judgment the public convenience and necessity may require. After issuance of such certificate, and not before, the carrier may, without securing approval other than such certificate, comply with the terms and conditions contained in or attached to the issuance of such certificate and proceed with the construction, extension, acquisition, operation, or discontinuance, reduction, or impairment of service covered thereby. Any construction, extension, acquisition, operation, discontinuance, reduction, or impairment of service con-

trary to the provisions of this section may be enjoined by any court of competent jurisdiction at the suit of the United States, the Commission, the State commission, any State affected, or any party in interest."

SEC. 5. Section 214 (d) of the Communications Act of 1934, as amended, is hereby amended to read as follows :

"(d) The Commission may, after full opportunity for hearing, in a proceeding upon complaint or upon its own initiative without complaint, authorize or require by order any carrier, party to such proceeding, to provide itself with adequate facilities for the expeditious and efficient performance of its service as a common carrier and to extend its line or to establish a public office; but no such authorization or order shall be made unless the Commission finds, as to such provision of facilities, as to such establishment of public offices, or as to such extension, that it is reasonably required in the interest of public convenience and necessity, or as to such extension or facilities that the expense involved therein will not impair the ability of the carrier to perform its duty to the public. Any carrier which refuses or neglects to comply with any order of the Commission made in pursuance of this paragraph shall forfeit to the United States \$100 for each day during which such refusal or neglect continues."

#### 4. SECTION 214, PRESENT LANGUAGE

Source: 47 U.S.C. 214 (1976).

##### **§ 214. Extension of lines or discontinuance of service; certificate of public convenience and necessity**

###### **(a) Exceptions; temporary or emergency service or discontinuance of service; changes in plant, operation or equipment**

No carrier shall undertake the construction of a new line or of an extension of any line, or shall acquire or operate any line, or extension thereof, or shall engage in transmission over or by means of such additional or extended line, unless and until there shall first have been obtained from the Commission a certificate that the present or future public convenience and necessity require or will require the construction, or operation, or construction and operation, of such additional or extended line: *Provided*, That no such certificate shall be required under this section for the construction, acquisition, or operation of (1) a line within a single State unless such line constitutes part of an interstate line, (2) local, branch, or terminal lines not exceeding ten miles in length, or (3) any line acquired under section 221 or 222 of this title: *Provided further*, That the Commission may, upon appropriate request being made, authorize temporary or emergency service, or the supplementing of existing facilities, without regard to the provisions of this section. No carrier shall discontinue, reduce, or impair service to a community, or part of a community, unless and until there shall first have been obtained from the Commission a certificate that neither the present nor future public convenience and necessity will be adversely affected thereby; except that the Commission may, upon appropriate request being made, authorize temporary or emergency discontinuance, reduction, or impairment of service, or partial discontinuance, reduction, or impairment of service, without regard to the provisions of this section. As used in this section the term "line" means any channel of communication established by the use of appropriate equipment, other than a channel of communication established by the interconnection of two or more existing channels: *Provided, however*, That nothing in this section shall be construed to require a certificate or other authorization from the Commission for any installation, replacement, or other changes in plant, operation, or equipment, other than new construction, which will not impair the adequacy or quality of service provided.

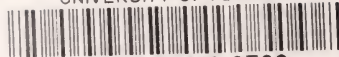
###### **(b) Notification of Secretary of Defense, Secretary of State and State Governor**

Upon receipt of an application for any such certificate, the Commission shall cause notice thereof to be given to, and shall cause a copy of such application to be filed with, the Secretary of Defense, the Secretary of State (with respect to such applications involving service to foreign points), and the Governor of each State in which such line is proposed to be constructed, extended, acquired, or operated, or in which such discontinuance, reduction, or impairment of service is proposed, with the right to those notified to be heard; and the Commission may require such published notice as it shall determine.

###### **(c) Approval or disapproval; injunction**

The Commission shall have power to issue such certificate as applied for, or to refuse to issue it, or to issue it for a portion or portions of a line, or extension thereof, or discontinuance, reduction, or impairment of service, described in the application, or for the partial exercise only of such right or privilege, and may attach to the issuance of the certificate such terms and conditions as in its judgment the public convenience and necessity may require. After issuance of such certificate, and not before, the carrier may, without securing approval other than such certificate, comply with the terms and conditions contained in or attached to the issuance of such certificate and proceed with the construction, extension, acquisition, operation, or discontinuance, reduction, or impairment of service covered thereby. Any construction, extension, acquisition, operation,





discontinuance, reduction, or impairment of service contrary to the provisions of this section may be enjoined by any court of competent jurisdiction at the suit of the United States, the Commission, the State commission, any State affected, or any party in interest.

**(d) Order of Commission; hearing; penalty**

The Commission may, after full opportunity for hearing, in a proceeding upon complaint or upon its own initiative without complaint, authorize or require by order any carrier, party to such proceeding, to provide itself with adequate facilities for the expeditious and efficient performance of its service as a common carrier and to extend its line or to establish a public office; but no such authorization or order shall be made unless the Commission finds, as to such provision of facilities, as to such establishment of public offices, or as to such extension, that it is reasonably required in the interest of public convenience and necessity, or as to such extension or facilities that the expense involved therein will not impair the ability of the carrier to perform its duty to the public. Any carrier which refuses or neglects to comply with any order of the Commission made in pursuance of this subsection shall forfeit to the United States \$100 for each day during which such refusal or neglect continues.

